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IN THE

Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-979

APPALACHIAN POWER COMPANY,
Appellant,

v.

THE PUBLIC SERVICE COMMISSION OF WEST VIRGINIA,
Appellee.

ON APPEAL FROM THE SUPREME COURT OF APPEALS
OF THE STATE OF WEST VIRGINIA

JURISDICTIONAL STATEMENT

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JURISDICTIONAL STATEMENT

Appalachian Power Company ("Appellant", "Appalachian" or "the Company") appeals from an order of the Supreme Court of Appeals of West Virginia ("West Virginia Court") entered on October 10, 1977 upholding certain orders of The Public Service Commission of West Virginia ("Commission"). Appellant submits this statement to show that the Supreme Court of the United States has jurisdiction of the appeal and should exercise its jurisdiction to determine the substantial questions presented.

Opinion Below

The order of the West Virginia Court entered October 10, 1977 is not officially reported. The orders of the Commission upheld by the West Virginia Court were issued May

6, May 9, July 29, August 26 and August 30, 1977 in the Commission's Case No. 8182 and are not officially reported. A copy of each order and notice referred to herein is included in the separate Appendix.

Jurisdiction

This appeal is brought to review orders of the Commission affecting rates charged for electric utility service to Appalachian's retail customers in the State of West Virginia.

Jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1257(2) to review a final judgment rendered on October 10, 1977 by the West Virginia Court. The West Virginia Court is the highest court of that State in which a decision could be had. The validity of certain statutes of West Virginia was drawn in question in the West Virginia Court on the ground of their being repugnant to the Constitution of the United States, and the decision of the West Virginia Court on October 10, 1977 was in favor of the statutes' validity.

The statutes which are the subject of this appeal are the Commission's order of May 6, 1977, as modified and affirmed as aforesaid. Appellant filed its Notice of Appeal with the Commission (the court possessed of the record) on October 14, 1977.

The following decisions sustain jurisdiction by appeal because the Commission's orders are "statutes" within the purview of 28 U.S.C. § 1257(2): *Atchison, Topeka & Santa Fe Railway* v. *Public Utilities Commission of California*, 346 U.S. 346, 348 (1953); *Bluefield Water Works & Improvement Co.* v. *Public Service Commission of West Virginia*, 262 U.S. 679, 683 (1923) (hereinafter "*Bluefield*"); *Lake Erie & Western Railroad* v. *State Public Utilities Commission of Illinois*, 249 U.S. 422, 424 (1919);

and *Grand Trunk Western Railway* v. *Railroad Commission of Indiana*, 221 U.S. 400, 403 (1911).

The following decisions further sustain jurisdiction by appeal on the basis that the October 10, 1977 order of the West Virginia Court was a "final judgment" of the highest court of that State in which a decision could be had and a "decision" in favor of the validity of the statutes drawn in question: *Atchison, Topeka & Santa Fe Railway* v. *Public Utilities Commission of California, supra* at 349; and *Napa Valley Electric Co.* v. *Railroad Commission of California*, 251 U.S. 366, 372-373 (1920).

In the event that the West Virginia Court order of October 10, 1977 is construed as not being a "final judgment" or as not being a "decision" in favor of the statutes' validity within the meaning of 28 U.S.C. § 1257(2), jurisdiction of this Court is invoked alternatively pursuant to 28 U.S.C. § 1257(2) to review by direct appeal the final order of the Commission rendered on July 29, 1977, as revised, modified and affirmed by its orders of August 26 and August 30, 1977.[1] In rendering these orders, the Commission acted in its quasi-judicial capacity by reviewing Appellant's petition for rehearing and was therefore the highest court of the state in which a decision could be had. In such capacity the Commission rendered its "decisions" in favor of the validity of the May 6 and May 9 orders which are "statutes" drawn in question on the ground of their repugnance to the Constitution of the United States. See *Prentis* v. *Atlantic Coast Line Company*, 211 U.S. 210, 223-226 (1908), which

1 *Nash* v. *Fla. Indus. Comm.*, 389 U.S. 235, 237 (1967). Docketing an appeal from these orders of the Commission was timely made because the 90-day period for docketing commenced at the same time as an appeal from the order of the West Virginia Court. No appeal could be taken prior to that date because the orders of the Commission were susceptible of being reviewed and reversed until that Court had acted. See *Andrews* v. *Virginian Ry.*, 248 U.S. 272, 275 (1919).

recognizes that a state public utilities commission may be a "court" within the meaning of federal statutory provisions, and *Atlantic Greyhound Corporation* v. *Public Service Commission of West Virginia,* 132 W. Va. 650, 659, 54 S.E.2d 169, 174 (1949), which recognizes that the Commission possesses quasi-judicial powers. Notice of Appeal from the Commission's order of July 29, 1977, as revised, modified and affirmed by its orders of August 26 and August 30, 1977, was filed with the Commission on January 3, 1978.

In the event that appeal is not considered the proper mode of review, Appellant requests that the papers upon which this appeal is taken be regarded and acted upon as a petition for writ of certiorari pursuant to 28 U.S.C. § 2103.

Questions Presented

I. Whether the Commission's rate order of May 6, 1977, as modified and affirmed, which precludes Appalachian from legally issuing additional long-term debt securities or preferred stock, violates the Fifth and Fourteenth Amendments of the United States Constitution and the criteria set forth in *Bluefield* and *Federal Power Commission* v. *Hope Natural Gas Co.,* 320 U.S. 591 (1944) (hereinafter "*Hope*").

II. Whether the Commission's rate order of May 6, 1977, as modified and affirmed, which precludes Appalachian from raising capital necessary for timely construction of facilities required for service to millions of consumers in numerous states, is an unconstitutional burden on or interference with interstate commerce in violation of Article I, Section 8, Clause 3 of the United States Constitution.

Statement

Appalachian, the largest public utility in West Virginia, is engaged in the production, transmission and distribu-

tion of electric energy at wholesale and retail, and serves more than 348,000 customers in the State. The rates which Appalachian charges its retail customers in West Virginia, and the terms and conditions of service affecting those customers, are regulated by the Commission.

Appalachian also serves over 330,000 customers in Virginia whose service is regulated by the Virginia State Corporation Commission. In addition, Appalachian serves 21 wholesale customers whose service is regulated by the Federal Energy Regulatory Commission (hereinafter "FERC"). Appalachian is a wholly-owned subsidiary of American Electric Power Company, Inc. (hereinafter "AEP"), a registered public utility holding company. Through their integrated generation and transmission system, AEP's operating subsidiaries serve directly territory having a population exceeding 6,000,000 people from east of the Blue Ridge Mountains to the shores of Lake Michigan—in Virginia, Tennessee, Kentucky, West Virginia, Ohio, Indiana and Michigan.

Appalachian filed with the Commission on March 31, 1975 tariff schedules based upon a calendar year 1974 test period which increased rates then in effect.[2] The new rates became effective on August 28, 1975, under bond and subject to refund. These rates produced approximately $41 million annually above the levels previously approved by the Commission. Hearings scheduled by the Commission commenced in July 1975 and were completed in August 1976. During these hearings and upon petition for rehearing, Appalachian submitted uncontradicted evidence which proved:

> (1) Minimum earnings requirements must be met in order legally to issue additional long-term debt securities or preferred stock;

2 At numerous times throughout the proceeding Appalachian attempted to have rates established on the basis of more current information. The Commission consistently refused.

(2) The credit rating of Appalachian's long-term debt and preferred stock was the lowest of any major electric utility in the United States;

(3) The construction program of Appalachian, which must be completed in a timely manner in order to provide adequate service to more than 678,000 customers in West Virginia and Virginia, requires the expenditure of more than $1 billion between 1976 and 1980; and

(4) Rate levels finally authorized by the Commission would prohibit Appalachian from legally issuing additional long-term debt securities or preferred stock.

On May 6, 1977—more than two years after Appalachian's filing—the Commission issued its order establishing for Appalachian one rate level for the period August 28, 1975 through April 30, 1976, and another rate level for the period on and after May 1, 1976. The first rate level allowed an increase of approximately $15 million annually or 36% of the requested rate increase. The second rate level allowed an increase of approximately $20 million annually or approximately 49% of the requested rate increase. Appalachian was directed to file new tariff schedules that would reflect the level of rates which the Commission found appropriate based on the 1974 test year. It was also ordered to refund to customers amounts collected in excess of such levels since August 28, 1975 which together with interest were approximately $45 million. In its May 6, 1977 order the Commission acknowledged that Appalachian must have an improvement in earnings in order to satisfy "the electricity demands of an energy-short public."[3] However, it did not even discuss the

3 Appendix, p. 30a.

Company's interest coverage requirements necessary to issue additional senior securities in order to finance the facilities necessary to meet those electricity demands.

On May 16, 1977 Appalachian petitioned the Commission for rehearing with respect to its order of May 6, 1977. Among other issues, Appalachian alleged in its petition that the end result of the Commission's order violates the Fifth and Fourteenth Amendments of the United States Constitution in that "the rates which the Commission established are legally insufficient to permit Appalachian to raise the money necessary to discharge its public duty to provide electric utility service."[4] The Chief Financial Officer of Appalachian and AEP, in an affidavit accompanying the petition, showed that the end result of the Commission's May 6, 1977 order was to reduce revenues to the point where the Company's interest coverage ratios were below the legal minimum necessary to issue any additional long-term debt securities.

On July 29, 1977 the Commission issued its order denying the rehearing sought in Appalachian's May 16th petition. Among other things, this order rejected the significance of interest coverage ratios in determining the adequacy of public utility rates. The Commission declared that coverage ratios are "no more than a security device used to restrain a company from imprudent future debt financing."[5] The Commission repeated its belief that the end result of its May 6, 1977 order is "eminently just and reasonable."[6]

On August 26, 1977 Appalachian filed its petition with the West Virginia Court seeking review of the Commission's

4 Petition for Rehearing, May 16, 1977, p. 2.

5 Appendix, p. 91a.

6 *Id.* at 92a. Pursuant to this order, Appalachian filed with the Commission on August 15, 1977 tariff schedules which were approved by the Commission on August 30, 1977.

orders of May 6 and July 29, 1977.[7] The petition and its accompanying note of argument renewed the constitutional claims asserted before the Commission and argued that the end result of the Commission's order failed to permit Appalachian to attract or even legally issue the senior capital necessary to discharge its public duties.[8] Appellant further asserted that the effect of the Commission's orders "places an undue burden upon and interferes with interstate commerce in violation of Article I, Section 8, Clause 3 of the United States Constitution. . . ."[9]

On October 10, 1977 the West Virginia Court, with one Justice dissenting, made and entered an order that in its opinion Appalachian had "not shown itself entitled to the relief prayed for in its said petition"[10] and on October 14, 1977 Appalachian filed its Notice of Appeal to this Court.

On October 26, 1977, after having been denied effective relief by both the Commission and the West Virginia Court upon its request for a stay of the Commission's orders, Appellant was granted a stay by The Honorable Chief Justice Warren E. Burger pending consideration of the Commission's response to Appellant's application for the stay. In the absence of this stay, Appellant would have

7 On August 26, 1977 the Commission ordered reopening of the proceeding to determine the reasonableness of a third tier rate level commencing May 1, 1977 (Appendix, p. 96a). The reopening is limited to consideration of Appalachian's increased coal expense since May 1, 1977. Accordingly any increase in rates subsequent to May 1, 1977 would be limited to the recovery of fuel expense already incurred and would not improve the Company's May 1, 1977 coverage levels. Even if the Commission authorizes full recovery of increased fuel expense since May 1, 1977, the related improvement in subsequent and current coverage levels would still not achieve the minimum levels required to issue senior securities.

8 Note of Argument, August 26, 1977, p. 16.

9 Petition, August 26, 1977, p. 7.

10 Appendix, p. 101a.

been required to make refund payments approximating $45 million before this appeal could be considered. After filing of the Commission's response and Appellant's reply thereto. The Honorable Chief Justice Warren E. Burger ordered a further stay on November 18, 1977, which has afforded Appellant an effective opportunity to submit this Jurisdictional Statement.

The Questions are Substantial

I.

The Commission's Orders Unconstitutionally Prohibit Appellant From Issuing Senior Securities.

The first question presented for the Court's consideration is the fundamental issue whether public utility rates which are so low as to preclude the utility from legally issuing additional long-term debt securities (except for refunding of maturing long-term debt issues under certain conditions) or preferred stock are violative of the Fifth and Fourteenth Amendments of the United States Constitution and the constitutional criteria set forth in *Bluefield* and *Hope*.

Appellant is unaware of any decision by this Court involving public utility rates which has specifically considered this question. However, as will be demonstrated, the minimum criteria of constitutional reasonableness which have been established in numerous decisions necessarily embrace the legal ability to issue additional long-term debt and preferred stock, the types of capital least expensive to the utility's rate-payers.

The resolution of this issue has far-reaching consequences for the more than 678,000 customers served by Appalachian in West Virginia and Virginia and approximately 2,000,000

customers served by operating subsidiaries of AEP in seven states. If Appalachian is unable to attract the new capital necessary to carry out its construction program in a timely manner, its ability to provide safe and reliable intrastate and interstate service will be jeopardized; and customers will face the strong likelihood of frequent and prolonged interruptions of electric utility service with their attendant economic and social disruptions.

A. The Need to Raise Additional Capital

The uncontradicted evidence before the Commission is that Appalachian is in the midst of a massive construction program which cannot be delayed if the Company is to be able to carry out its public utility service obligations during the next several years. The Company's construction program for the period 1976-80 is in the range of $1.2-$1.3 billion. To place this in perspective, it is an amount which exceeded Appalachian's net plant in service at December 31, 1975.

This vital construction program includes the completion by the winter of 1980/81 of a 1300-megawatt generating unit ("Project 1301") at a total cost approximating $600 million. Failure to place Project 1301 in service by the winter of 1980/81 will result in a dangerous capacity shortage for both Appalachian and all its sister operating companies in the seven-state AEP System.

The Federal Power Commission (now FERC) has concluded that electric utility industry planning should be based upon utilities' generating capacity exceeding customer demand by an average of 20% to assure reasonably reliable service.[11] By contrast, this winter Appalachian has the

11 Federal Power Commission: *The 1970 National Power Survey, Part I*, p. I-1-17. The *Survey* stated in part: "This conclusion was reached in light of the industry's increasing dependence on large generating units and the consequent need for large blocks of reserve capacity to offset unscheduled outages." *Id.*

capacity to serve a demand only 1% greater than the anticipated maximum demand of its customers. It will be able to meet the requirements of its customers only through reliance upon its sister companies. The record shows that by the winter of 1980/81 Appalachian's capacity, in the absence of Project 1301, will be more than 15% *below* its customers' projected requirements and the capacity reserve of the entire AEP System will be just 6.9%, a level not only entirely insufficient to assist Appalachian in meeting the projected demands of its own customers in West Virginia and Virginia but, beyond that, jeopardizing the reliability of service to the other AEP System customers in Tennessee, Kentucky, Ohio, Indiana and Michigan.

Other parts of Appellant's construction program are equally vital to its continued ability to provide reliable service. The Company must complete a major transmission line (at a cost estimated to exceed $70 million) by late 1979[12] in order to offset the likelihood of major and continuing blackouts to its customers in West Virginia south of Charleston and in neighboring portions of Virginia and Kentucky.

The evidence of the need for this enormous new construction was substantial and was uncontradicted by any party to the proceeding. In its decision, the Commission did not question the Company's construction requirements. The West Virginia Court made no mention of Appalachian's requirements for new plant.

B. The Ability to Raise Additional Capital

The uncontradicted evidence is that, even if the full amount requested in this case is allowed, Appalachian is able to generate internally through depreciation accruals and other sources only about $80 million per year to

12 The estimated cost of construction has since risen to more than $90 million with completion expected in 1980.

help meet its capital requirements when in 1978 its construction program is exceeding $360 million per year. Thus, Appalachian must be able to attract from external sources, including its parent, more than $280 million per year[13] to finance its construction program and complete the sorely needed facilities referred to earlier.

AEP, the parent, invested $80 million in the common stock equity of Appalachian during 1977. The Chief Financial Officer of Appalachian and AEP testified that the amount of such investment is restricted by market limitations on the sale of additional AEP common stock equity to the public and also by the equity requirements of AEP's other major operating subsidiaries. It is clear that even such an extraordinary infusion of capital (amounting to over 15% of Appalachian's total common equity capital), together with internally generated funds approximating $80 million per year, falls short of satisfying Appalachian's present annual capital requirements by approximately $200 million per year.

Appalachian, like electric utilities generally, uses three kinds of permanent capital to finance its enterprise—long-term debt, preferred stock, and common equity.[14] The typical electric utility uses long-term debt and preferred stock to finance approximately two-thirds of its capitalization, thus minimizing the overall cost of capital to its customers.

The minimum rate level necessary to attract additional common equity, the most expensive type of capital, cannot be quantified precisely and frequently is the subject of dis-

13 External financing requirements would increase if refunds are ultimately required to be made under the Commission's orders in this case.

14 This differs sharply from the type of financing used by the Bluefield Water Works & Improvement Company in 1923 and the Hope Natural Gas Company in 1944. Both utilities in those times financed their operations entirely with common stock. The total capitalization of Bluefield in 1923 was $312,000 in common equity; that of Hope in 1944 included $28,000,000 in common equity.

agreement among experts. Contrastingly, the minimum rate level necessary to issue additional long-term debt and preferred stock can be precisely quantified employing legal criteria included in Appalachian's Mortgage and Deed of Trust and its Debenture Agreement for long-term debt and its Restated Articles of Incorporation for preferred stock. They are substantially similar to the standards required to be met by the great majority of investor-owned electric utility companies operating in the United States and, in addition, are required by the Securities and Exchange Commission to be followed by operating subsidiaries of public utility holding companies.[15] With respect to long-term debt, the ratio of defined earnings to interest charges on all long-term debt of the Company, including annualized interest charges on additional debt securities proposed to be issued, must be at least 2.0 times for a 12-consecutive-month period in the 15-month period prior to the month in which the new debt securities are to be issued. With respect to preferred stock, the gross income of Appalachian for 12 consecutive months in the 15-month period prior to the month of issue must equal at least 1½ times the aggregate of the annual interest charges on all indebtedness and the annual dividend requirements on all preferred stock including the preferred stock to be issued.

The end result of the Commission's orders was to reduce Appalachian's coverage ratios substantially below the legal minimums outlined above. The evidence before the Commission demonstrated that the coverage associated with Appalachian's Virginia business exceeded the legal minimums; but that associated with West Virginia business,

15 See SEC Public Utility Holding Company Act Release Nos. 13,105 and 13,106 (February 16, 1956); 3 Fed. Sec. L. Rep. (CCH) ¶¶ 36,675 and 36,691.

1.80 times for the 12 months ending December 31, 1976,[16] was so low as to reduce the Company's *total* coverage levels below the legal minimum requirements.

C. The Commission's Refusal to Consider Capital Attraction Requirements

The Commission's decision of May 6, 1977 ignored the question of adequate coverage necessary to attempt to attract new senior capital. In rejecting Appalachian's request for rehearing, the Commission said that: coverage is not a test of confiscation; coverage is greatly affected by changes in capital structure; and coverage is no more than a security device to restrain a company from imprudent future debt financing.[17] The West Virginia Court made no reference to the consideration of coverage.

16 Appalachian's coverage has fallen even below this level in succeeding months, assuming application of the Commission's order on the same basis. For the 12 months ended August 31, 1977 the debt coverage associated with West Virginia jurisdictional business was 1.66 times and total coverage was only 1.80 times.

17 Appendix, p. 91a. The Commission's refusal to consider the coverage consequences of its decision is in sharp contrast to the decisions of other regulatory agencies and other courts. For example, the Mississippi Supreme Court has said:

> It [interest coverage] must be considered in fixing a rate for an operating utility because the rate must produce enough profit to enable it [the company] to maintain the coverages required; otherwise, bonds and preferred stock could not be issued as needed for expansion of facilities required to properly serve the certificated area of the utility. *Mississippi Power Co.* v. *Miss. Pub. Serv. Comm'n*, 291 So.2d 541, 547 (Miss. 1974).

Similarly the New York Public Service Commission in granting a temporary emergency increase in order that interest coverage would be .25 times *greater* than the legal minimum has said that "Denial of a temporary rate increase here would, in our judgment, pose an unacceptable threat to the continued provision of service. . . ." *Niagara Mohawk Power Corp.*, 14 N.Y.P.S.C. 1244, 1249 (1974).

The Commission's first rationalization cannot withstand even cursory analysis. This Court has said:

> The return should be reasonably sufficient to assure confidence in the financial soundness of the utility and should be adequate, under efficient and economical management, to maintain and support its credit and *enable it to raise the money necessary for the proper discharge of its public duties. Bluefield, supra* at 679. (emphasis added)

If the minimal constitutional criteria for public utility rates include raising ". . . the money necessary for the proper discharge of its [the utility's] public duties," the plain meaning of this standard includes being able legally to issue the two least expensive types of permanent capital, long-term debt and preferred stock.

The Commission's second rationalization for ignoring a utility's coverage in establishing rates says nothing more than had Appalachian financed differently in the past, its coverage might be different today. The rationalization ignores totally that Appalachian cannot finance today and that at no time in the Commission's continuing regulation of Appalachian has it questioned the reasonableness of Appalachian's capital structure and no evidence has been offered to suggest that the Company's capital structure is unreasonable or unusual. The current capital structure of Appalachian, including an approximately 60% long-term debt ratio, results from the Company's efforts to finance through debt issues, the least expensive form of permanent capital, to the maximum extent practicable and prudent.[18]

18 To the extent Appalachian's debt may be somewhat higher than the Commission, on a *post hoc* basis, might prefer, the greater level of interest charges, being deductible for income tax purposes, reduces Federal income taxes and, to the same degree, the revenues required from customers. It is ironic that the Commission has no difficulty accepting this revenue reduction stemming from the use of debt financing but balks at the thought of making debt financing, prospectively at least, practicable.

The Commission's third rationalization that coverage is a security device to restrain imprudent future debt financing, of course, is partly true. What the Commission ignores is that the predominant reason future debt financing would be imprudent and would be unlawful is the unconstitutional rate levels established by the Commission. In effect the Commission is establishing rate levels which make it both financially imprudent and legally impossible for the utility to attract the capital necessary to carry out its public duties. This *post hoc* rationalization is effectively a Commission acknowledgment that the rates which have been established fail to meet the standards which this Court has established in *Bluefield* and *Hope*.

D. Impairment of Appalachian's Credit Standing

Appalachian's credit in the marketplace where it must compete to attract capital has been seriously eroded by the Commission's actions. Appalachian's senior securities are rated in the lowest category of any major electric utility in the United States. Standard & Poor's rates the Company's first mortgage debt and preferred stock BBB– and its debentures BB–. Moody's rates Appalachian's first mortgage debt Baa and the debentures Ba.[19] Appalachian's credit standing has been undermined to the point where its first mortgage bonds are not legal investments for savings banks in at least eight states. Since many state pension funds are restricted by law to investing in securities that

19 Until February 1975 the Company's long-term debt and preferred stock were rated A by both rating agencies. Standard & Poor's defines BBB bonds as follows:

> The BBB, or medium grade category is borderline between definitely sound obligations and those where the speculative element begins to predominate. These bonds have adequate asset coverage and normally are protected by satisfactory earnings. Their susceptibility to changing conditions, particularly to depressions, necessitates constant watching. Marketwise, the bonds are more responsive to business and

Footnote continued on next page

are legal investments for savings banks, the failure of Appalachian's first mortgage bonds to qualify as such legal investments is a further restriction on the Company's financing capability.

Recent downgradings of Appalachian's securities are directly attributable to the decisions of the Commission. Standard & Poor's explained why it reduced its ratings from BBB to BBB– in April 1976:

> *In view of the less than adequate rate relief granted the company over the past several years* particularly in West Virginia, *the sizable amount of revenues currently being collected subject to refund, and the high percentage of long-term debt in its capitalization, we have changed the rating on all outstanding First Mortgage Bonds of Appalachian Power from 'BBB' to 'BBB–' and accordingly have rated this issue 'BBB–'.* (emphasis added)[20]

II.

The Commission's Orders Unconstitutionally Burden Interstate Commerce.

The second question presented for the Court's consideration is whether rates which are so low as to preclude Appalachian from raising capital necessary for timely construction of facilities required for service to millions of

Footnote continued from previous page

> trade conditions than to interest rates. This group is the lowest which qualifies for commercial bank investment. Standard & Poor's Corporation: *Bond Guide*, September 1976, p. 6.

In contrast:

> Bonds given a BB rating are regarded as lower medium grade. They have only minor investment characteristics. In the case of utilities, interest is earned consistently but by narrow margins. In the case of other types of obligors, charges are earned on average by a fair margin, but in poor periods deficit operations are possible. *Id.*

20 Standard & Poor's Corporation: *Fixed Income Investor*, April 17, 1976, p. 760.

consumers in numerous states are an unconstitutional burden on interstate commerce in violation of the Commerce Clause.

The result of Appalachian's financial inability to carry out its construction program in a timely manner does not cease with the impairment of service to West Virginia consumers whose service is regulated by the Commission. It extends directly to Appalachian's 330,000 retail customers in Virginia whose service is regulated by the Virginia State Corporation Commission. It extends directly to Appalachian's 21 firm wholesale customers in Virginia, West Virginia and Tennessee (which in turn serve at least 109,000 retail customers) whose service is regulated by the FERC. It has a profound impact upon service to consumers of electricity in all jurisdictions served by subsidiaries of AEP. In short, the financial inability of Appalachian to carry out its construction program in a timely manner which directly results from the Commission's decision jeopardizes an adequate supply of electric energy to millions of consumers in numerous states.

Appalachian is, in the Commission's words, "one of the main sources of power generation and transmission for the American Electric Power System, of which it is an integral part" and "supplies wholesale electric service both within and outside of its retail market areas directly and indirectly by bulk transmission or displacement", which is done "not only through the integrated AEP system, but also through 26 major electric utility supply systems which make up the regional grid known as the ECAR (East Central Area Reliability) group and through system interconnected, non-ECAR electric utilities (TVA, Carolina Power & Light, Duke Power, Commonwealth Edison, Illinois Power, Central Illinois Public Service Company)."[21]

21 Appendix, pp. 3a and 4a.

The advantages of Appalachian's participation in the coordinated planning and construction of facilities on the multi-state AEP System have been aptly recognized by the Commission:

> Other than distribution facilities, most of Appalachian's construction of generation, transmission and other facilities is planned on an AEP *system* basis of need and *not* solely on the needs of Appalachian Power Company customers. In addition, the construction of facilities by Appalachian and the said ECAR and non-ECAR electric utilities are planned on a coordinated, timed basis. The advantages of a coordinated group of power systems to the assurance of adequate, reliable and continuous public service are well known. (emphasis in original)[22]

The capacity shortages which may shortly occur in the geographical area served by Appalachian and neighboring utilities recently have been confirmed. The National Electric Reliability Council (NERC) determined in July 1977 that generation deficits could begin in the ECAR region in 1981—which assumes the completion of Project 1301 by the winter of 1980/81—and in adjoining regions from 1979 to 1985.[23]

There can be no question that Appalachian is engaged in interstate commerce as it transmits electrical energy across state lines.

22 Appendix, p. 4a.

23 The National Electric Reliability Council: *7th Annual Review of Overall Reliability and Adequacy of the North American Bulk Power Systems* (July 1977), p. 7. NERC is a voluntary organization, formed in 1968 as a consequence of the Northeast blackout, with the stated purpose: ". . . further to augment the reliability and adequacy of bulk power supply in the electric utility systems of North America." (*Id.* at inside front cover) It consists of nine Regional Reliability Councils and encompasses essentially all of the power systems of the United States and the Canadian systems in Ontario, British Columbia, Manitoba and New Brunswick.

> In transmitting [electrical energy] across the state line, [the utility] is engaged in interstate commerce, and state legislation in respect thereof is subject to the paramount authority of the commerce clause of the federal Constitution.[24]

The Commission's orders impose an impermissible burden on and interference with this interstate commerce by prescribing rates so low that timely completion of the Company's construction of its portion of the planned AEP system-wide construction program is imperiled.

The case of *Southern Pacific Co.* v. *Arizona,* 325 U.S. 761 (1945), is compelling. This Court found that Arizona legislation limiting the length of trains operated in that State contravened the Commerce Clause. The Court determined in reaching this decision that Congress had not superseded state regulation of train lengths by the Interstate Commerce Act, as amended,[25] and that a weighing of state and federal interests would be required. As stated by Mr. Chief Justice Harlan F. Stone,

> For a hundred years it has been accepted constitutional doctrine that the commerce clause, without the aid of Congressional legislation, thus affords some protection from state legislation inimical to the national commerce, and that in such cases, where Congress has not acted, this Court, and not the state legislature, is under the commerce clause the final arbiter of the competing demands of state and national interests. (citations omitted)[26]

In the instant case, though Congress has occupied under the Commerce Clause that portion of the regulatory area prescribed by Part II of the Federal Power Act, as amended,[27] Congress has not superseded all state regulation which may affect interstate commerce. However, where the

24 *Utah Power & Light Co.* v. *Pfost,* 286 U.S. 165, 182 (1932).
25 49 U.S.C. § 1 *et seq.*
26 *Southern Pacific Co.* v. *Arizona, supra* at 769.
27 16 U.S.C. § 824(a), *et seq.*

Commission has overstepped the bounds of reasonableness, this Court, as "the final arbiter", must engage in "appraisal and accommodation of the competing demands of the state and national interests involved."[28] The Commission's orders impose a serious burden on interstate commerce conducted by Appellant and interpose a substantial obstruction to the national policy proclaimed by Congress "of assuring an abundant supply of electric energy throughout the United States with the greatest possible economy and with regard to the proper utilization and conservation of natural resources."[29]

The decision of the Commission, if not reversed, will at a minimum result in the delay of major construction projects. That delay substantially increases the cost of those projects, a cost which must be absorbed by ratepayers in Virginia as well as in West Virginia.[30] In short, the Commission has set rates which are so low that, by impeding Appalachian's completion of its share of the AEP System's planned, timed construction program, the rates injure Appalachian's Virginia and FERC customers and the ultimate consumers of electric energy in other states.

Clearly, if the Commission had ordered Appalachian to sever its high-voltage transmission lines that carry needed electric energy to Virginia, and to and from Ohio and other neighboring states, so that Appalachian's electric system would have been isolated entirely within the State of West Virginia, there would be an unconstitutional interference with interstate commerce. In ordering rates which jeop-

28 *Southern Pacific Co.* v. *Arizona, supra* at 769.

29 Federal Power Act, 16 U.S.C. § 824a(a); see also *Southern Pacific Co.* v. *Arizona, supra* at 773.

30 For example, the delay which already is taking place in the construction of Project 1301 has increased the total cost of that project by about $160 million which in turn increases the rates which the customers must pay for that plant over the life of the plant by approximately $650 million.

ardize an adequate supply of electric energy to millions of consumers in numerous states the Commission is effecting exactly such an unconstitutional result.

If each individual state served by an integrated electric utility system, and offered the advantages of system-wide planning by that integrated system, could elect to cripple any participating utility located within its borders for the sake of short-term, rock-bottom rates, then such pools, encouraged by Section 202(a) of the Federal Power Act, soon would become meaningless and our Nation's power grid system would become a shambles of parochially insulated utilities. The public interest requires an appraisal and accommodation by this Court of the competing demands of the state and national interests.

Conclusion

The sum of the Commission's unconstitutional regulation can be stated succinctly—Appalachian's credit standing has been impaired, its ability to attract additional senior external capital has been eliminated and, accordingly, the supply of electric energy to millions of consumers in numerous states has been jeopardized.

In the past, this Court has noted that the determination "of 'just and reasonable' rates, involves a balancing of the investor and the consumer interests."[31] Appalachian's financial integrity has already been so impaired that a fair balance cannot be struck in this case. Rather, in this appeal the paramount interest is that of millions of consumers to obtain service through an adequate supply of electric energy. The energy crisis today is clearly among the most serious problems facing the country. The President of the

31 *Hope, supra* at 603.

United States has designated it his first priority and has called it "the moral equivalent of war".[32] Manifestly an adequate supply of electric energy is essential to sustain the economic heartbeat and social well-being of the Nation.

This Court should note probable jurisdiction, or, in the alternative, vacate the final orders appealed from and remand the case for such further proceedings as are necessary to permit Appellant an opportunity to earn a constitutionally adequate return, and this Court should grant Appellant such further relief as it may deem proper.

Respectfully submitted.

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January 6, 1978

32 N. Y. Times, April 19, 1977, at 24, col. 1.

Supreme Court, U. S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-979

APPALACHIAN POWER COMPANY,
Appellant,

v.

THE PUBLIC SERVICE COMMISSION OF WEST VIRGINIA,
Appellee.

ON APPEAL FROM THE SUPREME COURT OF APPEALS
OF THE STATE OF WEST VIRGINIA

APPENDIX TO JURISDICTIONAL STATEMENT

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PUBLIC SERVICE COMMISSION OF WEST VIRGINIA
CHARLESTON

At a session of the PUBLIC SERVICE COMMISSION OF WEST VIRGINIA at the Capitol in the City of Charleston on the 6th day of May, 1977.

CASE No. 8182

APPALACHIAN POWER COMPANY, a corporation.

In the matter of increased
rates and charges.

PROCEDURE

On March 31, 1975, Appalachian Power Company, a corporation (hereinafter "Appalachian" or "company"), filed its tariff designated P.S.C. W. Va. No. 3, cancelling P.S.C. W. Va. No. 2, stating increased rates and charges and certain modified rate designs for furnishing electric service in the entire territory served by it in the State of West Virginia, to become effective May 1, 1975. This filing included accounting data required by our Tariff Rule 42 based on a calendar 1974 test year.

By order entered on April 4, 1975, Appalachian was made respondent to this proceeding and pending investigation, hearing and decision said revised tariff was suspended and the use of the rates and charges stated therein deferred until August 28, 1975. It was further ordered that if the case had not been finally decided at the expiration of the aforesaid suspension period, such rates and charges applied for could not be placed into effect until a bond in the amount of Thirty Million Six Hundred Thousand Dollars ($30,600,000) with interest thereon, be given and approved by the Commission.

By order entered on June 3, 1975, the matters involved herein were set for hearing in the Commission's Hearing Room at the Capitol in the City of Charleston on July 21, 1975, at 9:30 a.m., EDT, and the company was required to give proper notice to the public.

By order entered on August 18, 1975, the Commission set the interest rate on refunds secured by the bond at 7¾%.

Proper notice was given and hearings were held on the following dates: July 21, 27, and 30, 1975 (consolidated with Appalachian Cases Nos. 7083—Reopened, 8192 and 8235); August 5, 1975; January 12 and 13, April 21, 22 and 23; June 7; July 12 and 13; August 10, 11, 12 and 31, 1976.

At the various hearings herein the company was represented by Charles R. McElwee and Samuel M. Sugden, attorneys at law, and the company's testimony was adduced from sixteen witnesses. The staff was represented by E. Dandridge McDonald, attorney at law, Legal Division; George R. Heath, Laxmi N. Mehra, David Ellis, and Robert Stier, Division of Accounts, Finance and Rates; and C. William Wensyel, Division of Engineering. Three witnesses were presented by staff. Attorneys for various intervenors were: Robert R. Rodecker, representing Appalachian Research & Defense Fund, Inc., Mercer County Economic Opportunity Corporation, and McDowell County Consumer Action Council, Inc.; Vincent V. Chaney and Michael T. Chaney, representing the City of Charleston and the City of South Charleston; T. D. Kauffelt, representing FMC Corporation; and John C. Lobert and C. E. Goodwin, representing ACF Industries, Inc., American National Rubber Company, Houdaille Industries, Inc., Huntington Alloys, Inc., Chemetron Corporation and Owens-Illinois, Inc. Mrs. Lucille Gillespie appeared for the Kanawha Valley Baptist Association, Clendenin, West Virginia, as a protestant. There were many protests.

Two witnesses were presented by intervenor, FMC Corporation; one witness appeared on behalf of low-income intervenors; one witness appeared on behalf of Owens-Illinois and one on behalf of Huntington Alloys, Inc.

On January 9, 1976, Appalachian filed its "Application for Interim Amendment to Appalachian's W. Va. P.S.C.

Tariff No. 3" requesting authority to credit .25074¢ per kilowatt hour for all service from August 28, 1975, through July 31, 1976. The reduction by "Rider A Credit Surcharge" (Original Sheet No. 18) resulted from the company's assessment that the embedded fuel cost component in the proposed rates should be reduced from 123.5¢ per Mbtu to 105¢ per Mbtu, and the application recited that the refund would include interest at 7¾% until paid.

On January 13, 1976, the Commission entered an order approving the application upon the condition, agreed to by Appalachian at a hearing held the same day, that the reduction in rates would continue until further order of the Commission, and would not terminate automatically on July 31, 1976, as proposed in the application.

Certain demand, energy and revenue data requested during the sessions ended August 31, 1976, were filed subsequently. Briefs were filed as to many of the issues before us, with the Appalachian's reply brief filed November 9, 1976.

Preliminary Comment

Background—Perspective

Appalachian is the largest public utility regulated by this Commission in terms of revenues received from West Virginia citizens. It brings the blessings of electric service to over 336,810 residential, commercial, industrial and institutional (churches and schools) customers located in 21 counties in the southern half of West Virginia. In addition, Appalachian is one of the main sources of power generation and transmission for the American Electric Power System, of which it is an integral part. The AEP system directly serves over 6 million customets [sic] in the States of Indiana, Ohio, Kentucky, Tennessee, Michigan, Virginia and West Virginia. Appalachian serves over 656,000 customers at retail in Virginia and West Virginia

and supplies wholesale electric service both within and outside of its retail market areas directly and indirectly by bulk transmission or displacement. This is done not only through the integrated AEP system, but also through 26 major electric utility supply systems which make up the regional grid known as the ECAR (East Central Area Reliability) group and through system inter-connected, non-ECAR electric utilities (TVA, Carolina Power & Light, Duke Power, Commonwealth Edison, Illinois Power, Central Illinois Public Service Company).

Other than distribution facilities, most of Appalachian's construction of generation, transmission and other facilities is planned on an AEP *system* basis of need and ***not*** solely on the needs of Appalachian Power Company customers. In addition, the construction of facilities by Appalachian and the said ECAR and non-ECAR electric utilities are planned on a coordinated, timed basis. The advantages of a coordinated group of power systems to the assurance of adequate, reliable and continuous public service are well known. Not so well known, however, is the fact that coordinated, "power center" controls over interlaced electric systems owned and operated by scores of cooperating affiliated and non-affiliated companies having generation capabilities, makes the fair, just and reasonable assignment of cost responsibility to various jurisdictions and classes of service a monumental regulatory task.

Background—Recent orders

On January 31, 1975, this Commission issued a comprehensive order allowing Appalachian a partial increase of requested higher rates on and after July 29, 1971, and providing for refunds. Since that date we have continued to regulate Appalachian to balance the interests of all segments of the public affected by its operations.

Highlights of this regulation progressed as follows:

On August 28, 1975, the Commission issued its order in Case No. 8192 denying Appalachian's request to impose a special surcharge on its West Virginia customers to recover unrecovered deferred fuel expenses occasioned by our order issued February 20, 1975, in Case No. 7945 terminating the automatic fossil fuel adjustment clauses in electric tariffs regulated by this Commission.

On October 10, 1975, we issued out interim order in Case No. 8235, which found that Appalachian had filed rates which resulted in an overrecovery of fossil fuel costs for the five-month period ended August 27, 1975, with the net overrecovery of $212,173 to be refunded in the subsequent Case No. 7083 (Reopened).

On October 20, 1975, we issued our order in Case No. 8229, denying Appalachian's attempt to exact a surcharge from its West Virginia customers alone to finance certain pollution control facilities at its Phillip Sporn generating plant.

On May 19, 1976, the Commission issued its order in Case Nos. 7083 (Reopened) and 8235, setting rates for the period January 1, 1974, through August 27, 1975, and providing for refunds. This set the lawful rates, underlying the proposed rates sought to be approved by this Commission in this Case No. 8182 for the period on and after August 28, 1975. See Appendix F, Column I.

As additional background to the foregoing Appalachian rate proceedings, this Commission on April 29, 1976, issued its certificate order in Case No. 8401, wherein Appalachian was authorized to construct a $72 million high voltage transmission line to move bulk power southeast from Cabell County to Wyoming County, West Virginia for eventual extension into its Virginia market area and beyond. Appalachian candidly admitted that its projected Culloden-Wyoming project would cause it to require

higher rates in the instant proceeding Case No. 8182. In our decision in Case No. 8401, we found that the appropriate apportionment of costs of this project to various rate jurisdictions and classes of customers for ratemaking purposes would remain an open question subject to determination in the appropriate rate proceedings.

The final backdrop to the rate drama now before us is our order issued September 15, 1976, in Case Nos. 7930 et al, which concerned certain of Appalachian's coal producing subsidiaries. We approved, with modifications, most, but not all, of the affiliated transactions as requested by Appalachian. However, we conditioned our modified approvals so as to be free in rate cases to be able to disallow excessive costs of purchases of coal produced by Appalachian's subsidiaries. This protection for Appalachian's West Virginia customers was found to be essential since the record in Case No. 7930, et al, indicated that beginning in early 1976, the price of affiliate coal in some months began to increase substantially above the price of coal purchased from non-affiliated suppliers, so that periodically the differential exceeded $3.00 per ton. We intend, in Case No. 8182 and future rate cases, to protect the public from excessive coal costs. In our said order in Case Nos. 7930, et al, we said:

> "In the circumstances of proven reserves and subsidiaries which are experienced in coal mine operations, there should be little reason for Cedar and Southern not to be able to sell their coal to Appalachian at a price lower than Appalachian is paying for coal purchased from its non-affiliated coal suppliers. In fact, except for bona fide *force majeure* occurrences, of which we are not aware, a continuation of such a differential in coal prices could lead us to conclude in an appropriate rate case that a higher coal price by affiliates is planned or is due to poor management.

> ". . . In the meantime, Appalachian should be induced by our present discussion of this issue to insist that its coal subsidiaries mine coal so as to sell it to Appalachian at the lowest possible reasonable price. Otherwise, Appalachain's [sic] payment of unreasonable coal prices to its affiliates must be absorbed by Appalachian as a deterioration of its earnings and will not be fully allowed as a recoverable item in its cost of service for rate-making purposes."

With these premises we turn to the task at hand of determining just, reasonable, and not unduly discriminatory rates for Appalachian covering the period beginning August 28, 1975, to the present and immediate future.

Issues

This proceeding contains the full sweep of usual rate case issues—rate base, allowable rate of return and going level and pro forma adjustments to operating expenses and other revenue deductions.

At the Commission's suggestion, the participants' [sic] attempted to narrow these issues by stipulation with only partial success, chiefly because of the threshhold [sic] issue of the propriety of using a 1974 test year to set rates beginning August 28, 1975.

The usual issues leading to a determination of over-all revenue requirements are supplementary to the equally complex issues of *jurisdictional* and *class* cost apportionment underlying the ultimate issue of proper rate level and rate design for the many different types of customers affected. The lowest possible reasonable revenue requirements [sic] is of immediate concern to the utility. However, West Virginia customers in each class are more concerned with how much *they* are going to pay as a fair share of Appalachian's total cost of rendering electric services to

the public located within and beyond the borders of West Virginia.

This Commission must *balance* these economic interests which pulsate with and against the meandering stream of the "public interest" in constantly changing patterns, much the same as the electricity flow which performs at the speed of light in amount, voltage and direction affected by billions of wise or wasteful human decisions to use or not to use power. Other regulatory bodies are called upon to perform these same tasks for the people within their jurisdictions. We now begin our difficult job to protect the interests of West Virginia with equity to all.

Test Year

On July 21, 1975, the evidentiary hearing began in Case No. 8182, together with Case Nos. 8192, 8235 and 7083 (Reopened). The rates in Case No. 8182 cover the most recent time period of the four cases that were consolidated, and is the sole remaining Appalachian rate proceeding now pending before this Commission.

At the outset of the first day of hearing in Case No. 8182, counsel for Appalachian agreed that its testimony presented on a 1974 test year would be the respondent's case on direct (T. 37-56). As the hearings progressed in 1975 to culminate in orders in the other three cases, the staff of the Commission performed its audit of Appalachian for Case No. 8182 on the basis of a 1974 test year.

On January 12, 1976, it was announced on the record (T. 529) that the staff's prepared testimony was to be served on the parties prior to February 24, 1976. In Case No. 7083 (Reopened), counsel for Appalachian recognized that "material must be audited" before final decision (T. 547). On the same day, at T. 562 and 564, the presiding officer stated:

> "We have begun to try the Case No. 8182 on a test period of 1974. The time has past for changing

> those test periods. The alternative of not sticking with this test period at this time when you are halfway through an evidentiary proceeding is that there would be a never ending rate case involving Appalachian Power if we were to permit this kind of leapfrogging of test year evidence and new test year we would never come to an end.
>
> ". . . and then if they want to protect themselves for the period beginning August 1, 1976, they have every right to come in here and file a new rate case which would then be heard on a test period that would be more applicable to that period."

On April 21, 1976, after the staff audit on a 1974 test year was completed, Appalachian sought to introduce evidence based upon a *1975* test year. The Commission refused to permit the company to deviate from its prior election to proceed on a 1974 test year, but left open the question of whether 1975 data would be admissible at the rebuttal stage of the hearing.

On August 10, 1976, the Commission adhered to its ruling that rates would be set on a 1974 test period, but admitted evidence based on a 1975 test period for the limited purpose of deciding the propriety of the adjustments made to 1974 test year data.

The Commission finds that its ruling was entirely proper, particularly in light of staff evidence based upon unaudited 1975 figures and proper adjustments, that there was no decline in rate of return on going-level projections for 1975 as compared with 1974. Moreover, Appalachian's unaudited 1975 data contained several improper adjustments. For example, it assumed approvals by this Commission which were not forthcoming, concerning the transfer of ownership of certain of its coal properties. We denied Appalachian's request to transfer such coal properties to its coal producer subsidiaries by order issued September 15, 1976, in Case Nos. 7930, et al. Also, in its 1975 test

year data, Appalachian adjusted its going-level expenses for both 1975 and 1976 wage and salary increases. This would render its 1975 projection incomparable to its 1974 test year data and would tend to understate the resulting 1975 rate of return.

As we have stated in the past, the selection of a particular test year to be used in ratemaking involves a discretionary judgment on behalf of the Commission.

When a utility seeks to depart from the test year it first elects to use in the evidentiary hearing for a more current 12-months period, the Commission must weigh the advantages of a more recent period against the disadvantages of delay in the administrative process required by a long recess for purpose of staff audit of the new period. In the instant case, as in our order issued May 19, 1976, in Case Nos. 7083 (Reopened) et al, we adhere to our ruling on a 1974 test year with limited reference to 1975 data, since we "must always protect the administrative process from abuse and bring rate proceedings to an end for the public good."

Due to the passage of time since the rates in question went into effect and the date of this order, we will fully protect Appalachian from any real or feigned unreasonable injury by setting rates in Case No. 8182 on a two-tiered basis — (1) for the period August 28, 1975, through April 30, 1976, and (2) for the period on and after May 1, 1976. Cf. *C & P Telephone Company, Case No. 7496,* order issued June 24, 1974, *W. Va. P.S.C. 61st Annual Report,* pages 204-224.

Comment

The starting point for our consideration of adjustments to test year 1974 costs is as follows:

	Per Books — Staff	
	Total Company	Allocated to West Virginia
Operating Revenues	$439,573,142	$187,641,566
Operating Revenues Deduction Operation and Maintenance Expense	$244,021,372	$ 97,757,987
Depreciation and Amortization	$ 40,357,524	$ 16,866,980
Taxes Other Than F.I.T. ...	$ 27,803,909	$ 15,138,692
Federal Income Tax	($ 191,105)	$ 1,907,377
Total Deductions	$311,991,700	$131,671,036
Net Operating Income	$127,581,442	$ 55,970,530
Average Rate Base	$1,131,301,490	$472,790,666
Rate of Return	11.28%	11.84%

Appalachian's evidence of per books costs differed from the results of the staff's more recent audit made after accounting adjustments for federal income tax expense and differences in jurisdictional allocations of costs to West Virginia. Moreover, Appalachian's rate base methodology was not comparable to that of the staff, thus distorting the comparability of resultant rates of return both before and after going-level and pro forma adjustments of staff and company.

The end result after various adjustments to a going-level by Appalachian and staff compare as follows:

	APPALACHIAN		STAFF	
	Total Company	Allocated to West Virginia	Total Company	Allocated to West Virginia
Adjusted Operating Revenues	$ 425,550,313	$180,880,505	$ 420,827,187	$176,085,074
Adjusted Operating Rev. Ded.				
Operation and Mn. Expense	$ 257,133,668	$ 96,120,982	$ 263,751,098	$105,990,991
Depreciation and Amortization	$ 46,364,714	$ 20,894,282	$ 41,558,747	$ 17,334,859
Taxes Other than F.I.T.	$ 31,608,703	$ 17,166,935	$ 30,829,056	$ 16,023,424
Federal Income Taxes	$ 11,270,218	$ 6,730,704	($ 1,893,176)	($ 737,846)
Total Deductions	$ 346,377,303	$140,912,903	$ 334,245,725	$138,611,428
Net Operating Income After Adjustments	$ 79,173,010	$ 39,967,602	$ 86,581,462	$ 37,473,646
Allowance for Funds Used During Construction	$ 4,672,345	$ 2,142,040	—	—
Total Operating Income Plus Allowance For Funds Used During Construction	$ 83,845,355	$ 42,109,642	$ 86,581,462	$ 37,473,646
Rate Base	$1,319,121,055	$595,076,068	$1,171,404,899	$488,448,552
Rate of Return	6.36%	7.08%	7.39%	7.67%

The staff going-level rate of return of 7.67% for West Virginia is calculated on an *average* rate base, while the Company's going-level rate of return of 7.08% is based upon a *year-end* rate base, plus full allowance for plant expenditures accounted for as Construction Work in Progress (CWIP), and the addition of an income allowance for funds used during construction (AFUDC).

Specific Adjustments

The foregoing indication of wide divergence in the positions of Company and staff must be resolved by decisions on several specific, subsidiary issues to reach a representative matching of allowable costs to projected test-year revenues to set rates for the periods beginning August 28, 1975, and May 1, 1976.

Since we have decided that 1974 is an appropriate test year to use in the circumstances of this case, we interpret Appalachian counsel's letter to staff counsel dated August 10, 1976, as an agreement to narrow certain specific issues to be decided to the following:

1) Allowable adjustment to going-level fuel expense and related revenue adjustment.
2) Adjustment to purchased power expense to offset effect of an obsolete Capacity Equalization Agreement among affiliates of the AEP system.
3) Depreciation expense—(a) certain anti-pollution plant and (b) rights-of-way.
4) Property tax expenses in three States.
5) Miscellaneous adjustments for 1976 expenses.
6) Rate base—(a) working capital, (b) year-end vs. average and (c) Construction Work In Progress.
7) Rate of return on rate base.
8) Federal Income Tax—(a) normalization-tax depreciation, (b) investment tax credit—level

and normalization, (c) consolidated tax savings and (d) pro-forma revenue tax effect.

9) Jurisdictional cost apportionment.

10) Class of service cost apportionment.

11) Rate level and rate design.

1. *Adjustments Related to Fuel Expense*

One of the most difficult and substantial issues in this case is the determination of a reasonable level of fossil fuel expenses for the test year to set rates for the periods which began August 28, 1975, and May 1, 1976.

Appalachian urges a going-level *fuel* expense at $1.05 per million Btus *estimated* as the average for the period March 1976 through December 1977, which period began six months after the date the proposed rates were put into effect. Staff presented evidence to support an adjustment of *coal* expense to $221,257,082 (at $.998416 per million Btus) based upon the period September 1975 through April 1976, which period began eight months after the end of the test period and covered the immediate eight-month period after the requested rates were put into effect under bond. The effect of this staff adjustment would be to reduce actual test year per books coal expense from $225,966,126 (at $1.01966 per million Btus) to $221,257,082. These costs are for coal expenses only and are not the total Account 501 fuel expense, which includes other fuel and handling expenses. The comparable staff weighted average total Account 501 unit cost would be about $1.02 per million Btus.

We find that $1.00 per million Btus is a reasonable level of coal expense for determining the *first-tier* rates covering the period August 28, 1975, through April 30, 1976. In our order issued October 10, 1975, Case No. 8235, we found that the actual unit fuel cost for the period April through August 1975, was $1.03604 per million Btus. Coal prices

declined and stabilized somewhat in mid-1975. Thus, by adopting the staff approach the customers of Appalachian are given the benefit of the recent "softening" in the coal market.

Appalachian's proposed adjustment to $1.05 per million Btus is rejected, because rates based on such "estimated" fuel costs would permit Appalachian to recover substantially more than its actual fuel costs for that eight months period in which the first-tier rates are made firm.

However, for the purpose of determining *second-tier* rates for the future on and after May 1, 1976, we cannot ignore the relentless march of inflation on the price of coal. As disclosed by the record, we monitor the price of coal (Account 151) through the monthly fuel reports filed by Appalachian under Code 24-2-14. We have noted that beginning in the last two months of 1976 and the first two months of 1977, the price of coal purchased from non-affiliated suppliers is increasing, possibly due to wage escalations under the UMWA union contract.

The evidence of record indicates that the 1974 test year cost of affiliated coal was *lower* than non-affiliated coal purchases. This relationship has now reversed so that affiliated coal is currently *higher* than "outside" purchases. As previously stated we have warned Appalachian that we would protect the public from excessive coal costs. In Case Nos. 7930, et al, by order issued September 15, 1976, we cautioned Appalachian that it may be made to absorb any unreasonable differential between the price it pays for coal to its affiliated suppliers and to its non-affiliated coal producers.

However, we need not go outside the record to determine a reasonable level of fuel expense for setting rates to be lawful on and after May 1, 1976. In our judgment, based on the evidence, confirmed by our analysis of monthly fuel reports under Code 24-2-14, we find that $1.04 per million Btus or $230,472,530 is a reasonable level of coal expense

to be allowed in the costs to be recovered by the *second-tier* rates. This is greater than Appalachian's actual 1974 test year coal expense of $225,966,126.

Counsel for Appalachian objected to staff's *revenue* adjustment No. 3, which reflected the "roll-in" to base rates of .998¢ per KWH occasioned by our termination of the fuel adjustment surcharge as of April 1, 1975. Appalachian appears to argue that the going-level fuel cost adjustment should be $1.05 per $\overline{M}$Btus, rather than $.998416 $\overline{M}$Btus, and if so, the revenue adjustment would be erroneous. Such an objection is not well taken, because we are here considering a going-level adjustment which the staff made in order to reflect rate levels in effect prior to the filed rates proposed herein. Our allowance of $1.04 per $\overline{M}$Btus for the second-tier rates will increase expenses and any revenue deficiency resulting from higher fuel expenses will cause a resultant increase in allowable revenues to cover the higher costs.

2. *Purchased Power Expense Adjustment to Reflect Effect of Renegotiated Capacity Equalization Agreement Among AEP Affiliates*

The affiliates of the AEP system are each in different stages of growth. By virtue of the fact that growth of steam generation is on a *system*-basis rather than a *company*-basis, excess capacity on one AEP company is made available to its sister companies on a shared basis pursuant to agreement setting up a formula rate, allocating portions of the operating and capital costs of the excess capacity. This agreement among affiliates is known as the "Capacity Equalization Agreement". It is regulated by the Federal Power Commission.

During the test year Appalachian was a capacity-excess company and received revenues from its sister companies based in part upon a formula which contemplated an unreasonably low investment per kilowatt of generating capacity ($100 per KW of capacity) as compared with the

actual investment of in excess of $150 per KW of capacity during 1974. The AEP companies recognized this underpricing and in June 1975 filed with the FPC its Modification 3 to the Capacity Equalization Agreement.

Recognizing a need for going-level adjustment to power production expense on a known and measurable basis, the staff adjusted test year per books power production expenses by crediting revenues of $30,873,058 from AEP affiliates, instead of $26,209,579, against total power production expenses of $227,940,896, for allowable power production expense $3,939,615 less than it would have been otherwise.

The Company contends that the staff adjustment is improper not because the capacity equalization rate had been increased in June 1975, but because at some point subsequent to the test year Appalachian purportedly became a capacity-deficient company in the AEP system. The Company's contention is not well taken, because even when it is a net purchaser of power from its affiliates at a higher capacity equalization rate, it will have the benefit of substantial increased revenues from the resale of its purchased power under the Capacity Equalization Agreement.

It may well be that the Modification 3 rate formula provides charges which are still too low as among affiliates. This could be determined after cost apportionment studies. No cost apportionment studies were presented in the record going to classes of service within the Federal sphere of jurisdiction. However, since the AEP companies filed the Modification 3 rate formula with the FPC, Appalachian could not argue that the staff adjustment was excessive or was not based on a known and measurable change occurring soon after the end of the test period.

We find that the staff adjustment to per books purchased power expense to reflect a going-level reduction caused by an understatement of capacity equalization revenues is proper and reasonable.

3. *Depreciation Expense Adjustments*

Pollution Control Facilities

In late 1974 and 1975, Appalachian added pollution control facilities to its Glen Lyn and Clinch River generating plants. On the basis of an investment of $39,741,706 at August 31, 1975, staff would allow an adjustment to depreciation expense of an additional $1,231,993, derived from applying a 32-year service life or a depreciation rate of 3.1% to the investment.

The Company, on the other hand, urges the Commission to allow a depreciation expense adjustment, at much higher depreciation rates, amounting to $5,008,508 derived from the estimated remaining lives of the respective generating units to which the electrostatic precipitators are attached varying from 3 years remaining life for Glen Lyn Unit No. 5 to 21 years for Clinch River Unit No. 3.

This Commission has refused to permit utilities to increase their depreciation rates and expense in contemplation of a rate case. See *Cabot Corporation, Case No. 8289,* order issued October 6, 1976, at page 10. Changes in depreciation rate may be proper in order to protect invested capital which is subject to rapid physical deterioration, obsolescence or functionally reduced service life. However, there is always the temptation for a utility to increase its depreciation rates in order to attempt to justify an increase in rates and charges to its customers. For this reason, in our new Rules of Practice and Procedure dated March 1, 1977, we have adopted Rule 20 covering changes of depreciation rates, so as to ease the problem of how to reconcile accounting changes required by good engineering, accounting and management principles, with proper ratemaking. The intent is to establish proper depreciation rates prior to and independent of ratemaking to the extent permitted by the circumstances.

Staff argues persuasively that Appalachian's position is too extreme, because, for example, it would assume un-

realistically that Appalachian would have spent $7,000,000 in 1974 for anti-pollution devices on its Glen Lyn Unit No. 5 and would retire the same from service early in 1977.

We find that the staff position is proper and that Appalachian has failed in its burden of proof to establish depreciation rates which are higher than the 3.1% composite generating plant depreciation rate used by the company for the units to which the electrostatic precipitators are attached.

Rights of Way

Appalachian seeks our approval for an adjustment to its depreciation expense by an additional $1,010,000 for depreciation on transmission rights of way and distribution rights of way. Traditionally, land, including rights of way encumbering realty, are not depreciable, for other than tax or special statutory purposes in certain circumstances. There is nothing of record to support the Company position on this issue. The claimed depreciation expense does not fall within any tax or special statutory exception to the general rule excluding rights of way from depreciation expense accounting. To the contrary, the claimed depreciation expense has never been recorded on Appalachian's books and the record is silent on the nature of the rights of way, their estimated service life and the method of reaching the claimed depreciation expense. We find that Appalachian's claim for depreciation expense adjustment is without merit and is rejected.

4. *Property Tax Expense Adjustments*

In Appalachian counsel's letter narrowing the issues in controversy, he took the position that regardless of whether the test year would be 1974 or 1975, "property taxes should reflect *actual* taxes paid in *1975*". However, this issue was not briefed by Appalachian. Pertinent evi-

dence shows real and personal property taxes to be as follows:

	1974		1975
	Per Books	Staff Adjusted	Per Books
West Virginia	$5,237,110	$ 7,405,577	$6,483,804
Virginia	3,922,844	5,229,582	3,431,101
Tennessee	31,542	34,128	36,647
Total	$9,191,496	$12,669,287	$9,951,552

We have selected 1974 as the test year and will approve the staff adjustments as made. The per books property taxes are as shown due to Appalachian's overaccruals of property taxes for prior years.

Property taxes are only one type of tax accounted for as "Taxes Other Than Federal Income". Other taxes, such as payroll taxes, gross receipts or business and occupation taxes and regulatory fees, will be further adjusted to reflect the effect of wage adjustments allowed in setting the second-tier rates to be approved, increases in the FICA tax base and revenue adjustments derived from the rates determined herein.

5. *Second-tier Miscellaneous Adjustments For 1976 Going-Level Adjustments To Expenses*

Because of the unique regulatory background involving Appalachian before this Commission and the necessary passage of time to afford full due process of law in our actions in this case, we are adopting the rare procedure of setting two different levels of rates in one numbered proceeding before us. We have already disposed of the most substantial subsidiary issue by finding above that the embedded cost of coal for determining rates to be in effect on and after August 28, 1975, through April 30, 1976, should be $1.00 per $\overline{M}$ Btus, and for the period on and after May 1, 1976, should be $1.04 per $\overline{M}$ Btus.

In addition, Appalachian urges that a going-level adjustment be made to the 1974 test year for (1) wage and salary increases put into effect April 1, 1975, and April 1, 1976; (2) postage rate increases which went into effect December 28, 1975; (3) medical insurance premium increases that took effect March 1, 1976; and (4) an FICA tax base increase effective January 1, 1976.

The record reveals that the magnitude of these additional operating expense adjustments would be as follows:

	Total Company
(1) Annualized Wage and Salary Increases:	
— effective April 1, 1975.....	$1,823,000
— effective April 1, 1976.....	2,684,000
(2) Postage Rate Increase.....	248,000
(3) Medical Insurance Premiums.....	343,000
(4) Increase in FICA Tax Base.....	181,000
Total	$5,279,000

In addition, a fifth adjustment was proposed by Appalachian of $1,531,000, representing a restoration of line maintenance expenses which were cut back in 1974, as an austerity measure to minimize cash outflow and to improve earnings. The test year expense reductions which should be restored to assure adequate service were detailed as follows:

80 line crews (412 men), outside contractors used in —ground line pole treatments	$ 187,000
— pole and tower painting	54,000
— overhead line maintenance	576,000
47 crews (147 men), outside contractors used in — tree and brush control.....	600,000
Related maintenance material costs.....	114,000
Total	$1,531,000

These five adjustments are found to be reasonable and proper and based on evidence establishing known and

measureable criteria and are to be allowed in determining the *second-tier* rates to be in effect on and after May 1, 1976. The April 1, 1976, wage increase, postage rate increase, medical insurance premium, and increase in FICA tax base are *not* allowed for the rate determination underlying the period August 28, 1975, through April 30, 1976, because their cost impact would not be substantial until the second-tier period.

We will allow for both the *first-tier* and *second-tier* periods and adjustment to the 1974 test period costs to reflect the annualization of wage increases that became effective April 1, 1975, in an amount of $1,823,000, and was recommended by staff as a proper going-level adjustment.

The adjustment of $1,531,000 in line maintenance expense, recommended by staff in its Exhibit No. 8, is allowed in both the first-tier and the second-tier rates so that in the future Appalachian will not be able to rely on a temporary austerity program to defer proper and necessary line maintenance required for adequate service to the public.

These adjustments are unusually liberal to the Company and are allowed in the determination of rates as described only in the context of the circumstances of this case affecting Appalachian and its customers. It is but one factor affecting our judgment, while realizing that such will be counter-balanced by our decisions on other subsidiary issues so that the end-result in rate-making will be fair, just and reasonable to all concerned.

6. *Rate Base*

This Commission has pointed out that "rate base", better described as "earnings base", is significant in ratemaking only as a tool to determine "allowable earnings" for a test period. In the "rate base—rate of return" method of ratemaking, the "allowable earnings" is the resulting product from the multiplication of "rate base" times "rate of

return". The allowable earnings are needed to retire debt, pay interest and dividends, and otherwise to be used in the business for construction or working capital. Such allowable earnings should also be adequate to permit the utility to finance reasonable expansion. Said "allowable earnings" are then subject to increase to recover "projected" income taxes associated therewith, by inclusion in the total cost of service to be recovered by the rates to be designed.

Except as to certain very small utilities and some governmental utilities, the "rate base—rate of return" method is the usual mode of cost-based ratemaking. This method uses projections of reasonable capital costs as but one component of the total reasonable costs (revenue requirements) allowed. The "end result" of just and reasonable rates are based upon these reasonable test year revenue requirements.

Although we discuss the two factors of "rate base" and "rate of return" separately and in precise numbers, we do so with an understanding of the limitations and interrelationships of certain concepts which affect our judgmental decisions. Evidence on the issues of rate base and rate of return are susceptible to a range of findings all of which have validity. Since the important consideration is the product of the two factors, rather than the factors themselves, our judgment in selecting precise numbers within a range of acceptable numbers are interdependent. Thus, there is a need to be fully aware of certain distinctions and the nature of statistical evidence. For example, there is a difference in concept and often a substantial variance in dollars between "rate base" and "total capitalization". "Rate base" consists of net plant (less customer contributions and tax deferrals) plus an allowance for working capital; whereas, "total capitalization" includes debt, deferred equity and common equity. Distinguishing these concepts, Appalachian's witness Brennan can show an actual, year end *total capital* of $1,397,451,000 as of Decem-

ber 31, 1974, and its witness Berg can sponsor a per books, year end *rate base* of $1,318,019,244, without being inconsistent. See Appendix A to this order. Likewise, it is not inconsistent for rate base witnesses to make going-level adjustments to change the test year rate base to another amount for purposes of fairness on the "matching" principle. It is partly for this reason that results of rate of return on capitalization studies are not the same as rate of return on rate base.

The concept of test year projections and adjustments to rate base costs, costs of service and revenues in *ratemaking* is a theorization based on facts in an attempt to reach a fair ideal matching of costs to revenue for the immediate future in order to prevent either excessively high or unreasonably low earnings. The Commission now and in the past has used such projected data in this fashion.

Proceeding now to the specific controversies over rate base items in this case, the Company urges as to (1) use a "year-end" rate base rather than a 13-month "average" rate base, (2) include in rate base *all* expenditures accounted for as "Construction Work in Progress" (CWIP), and (3) include in rate base an amount for cash working capital based upon an allowance of 1/8th of test year operating and maintenance expenses, excluding purchased power expense, but unadjusted for the lag experienced in payments for coal purchases.

The Commission has adhered to the average of 13-month balances method of ratemaking and the exclusion from rate base of most Construction Work in Progress, because it believes that the test year method of ratemaking should attempt to properly match the relationship between plant, expenses and revenues. We have allowed an exception to the general principle which excludes CWIP from the rate base in the case of CWIP expenditures for pollution control facilities, because such expenditures are (1) large, (2) required by governmental environmental regulation, (3)

non-revenue producing, and (4) operating cost increasing. The exception is made because of the equities involved and the same matching principle that supports the general rule. Such limited CWIP is allowed in rate base, so that the utility will be allowed to begin immediately to recover from ratepayers for substantial expenditures made involuntarily by the utility in compliance with governmental edict.

Both the year-end rate base and CWIP recommendations by Appalachian are rejected because, in the context of a substantial growth company, they tend to unduly accelerate the recovery of costs by mismatching capital costs for plant, which is just beginning to be or will be "used and useful" in the rendition of utility service, with test year billing units applied to adjusted revenues and costs.

In a growing company such as Appalachian, a *year-end* rate base would be larger than a rate base determined on an *average* monthly basis. The Staff shows a per books *average* rate base for 1974 as $1,131,301,490 to be adjusted to a going-level of $1,170,149,735 for total company.

Obviously, *any* allowable rate of return would produce higher earnings on a year-end rate base than on an average rate base for ratemaking purposes. As to a company with substantial growth in plant and sales, allowance of year-end rate base and *all* CWIP in rate base would tend to skew unreasonably a fair and representative relationship between revenues derived by application to lower test year billing units and higher capital costs for plant growth needed for greater future sales.

The Staff argues that exclusion of most CWIP from rate base is fair, since the Company can capitalize an Allowance for Funds Used During Construction (AFUDC) and recover such funds, including a return thereon, when the construction projects are completed and placed in service. Construction Work In Progress is a plant asset item on the balance sheet with no specifically related counter-entry in the total capitalization, either as debt or equity. The real

question is the extent to which present customers or stockholders should carry the burden of these CWIP expenditures for service to begin at some unknown date or dates in the future. We find that the Staff positions on these two subsidiary rate base issues are sound. We adhere to our prior precedents which require an average rate base, adjusted for year-end Construction Work In Progress dollars invested in pollution control facilities.

The working capital rate base issue is presented to us in the following manner. It is a standard principle that a utility should be allowed to earn a return on a reasonable level of cash working capital.

Working capital is not a constant or fixed percentage of rate base. Although it is sometimes approximated by formula or percentages, such mathematical exercises are valid only as an administrative convenience to be modified when results tend to be disproportionate under a fair analysis. Working capital is composed of three major components. The test year per books amounts as adjusted by Staff are as follows:

	Per Books		As Adjusted	
	Total Company	Allocated To W. Va.	Total Company	Allocated To W. Va.
	$	$	$	$
Materials and Supplies (Inc. Fuel)	63,051,604	25,224,455	63,051,604	25,224,455
Prepayments	985,651	408,848	985,651	408,848
Working Cash	15,362,671	6,290,961	19,810,607	8,059,853
Total Working Capital	79,399,926	31,924,264	83,847,862	33,693,156

The cash working capital component may be defined as the amount of cash required to be available to a utility for the payment of its operating and maintenance expenses which are incurred and paid for before operating revenues are sufficient to pay for such expenses. Theoretically, the investor is providing this cash for a short period of time

before the customer receiving service pays revenues to cover the expenses inherent in the service. The investor is allowed to earn a return on his investment used by the utility as cash working capital. Thus, the reason for the rule is tied directly to the lag period between the average time expenses are incurred and paid and the average time concomitant revenues are received by the utility. It can be argued that a regulatory body should be generous in allowance for cash working capital in rate base, in view of the fact that a utility has the legal obligation to perform continuous, adequate service to the public and cannot shut down and refuse to buy electricity or generating fuel to lessen the need for cash working capital. However plausible this argument, this West Virginia Commission must be neither generous nor niggardly, but must seek a balance and fair decision on this issue, as well as all issues, that affect the public servant and the public served.

In the past the Commission has used a modification of the FPC 45-day formula, whereby it has allowed as cash working capital 45/365 or ⅛ times the total operation and maintenance expenses after deducting purchased power expense. Purchased power expense is deducted on the premise that it does not represent an immediate cash outlay or does not have to be paid until close to or after the amounts involved have been collected from the customers.

In some cases, the Commission has allowed the utility to include fuel expense in the operating expenses to which the ⅛th factor is applied on the premise that there is a 45-day lag between the payment for the fuel and the receipt of revenues for the sale of electricity generated by the fuel. However, fuel expenses is [sic] such a large part of total operating expenses, that we should constantly review each utility's purchase and payment for fuel and receipt of concomitant revenues, to ascertain whether in fact a 45-day cash working capital requirement is realistic.

In this case, the staff audit revealed (based on August 1974 coal deliveries) that the Company was receiving revenues for service from 30 to 60 days after service, for an average of 45 days, while it was paying for coal purchased on an average of 29 days after it received the coal. Thus, deducting 29 days from 45 days, there would be a 16-day lag period during which the customer's money would not be available to pay for the fuel portion of service received. Therefore, Staff's adjustment to cash working capital was calculated upon a 16/365th, instead of a 45/365th or ⅛th, of fuel expense to reflect a lesser need of invested cash.

For these reasons we accept the staff methodology of calculating a reasonable allowance for working capital to be included in rate base.

7. Rate of Return

Cost of capital on Appalachian's *total capitalization* is but one of several guidelines to the Commission's judgmental decision on rate of return to apply to *rate base* for ratemaking purposes. We have previously discussed the differences in concept and dollars between (1) "total capitalization" used to estimate cost of capital and (2) "rate base—rate of return" in ratemaking. Thus, it would be improper to believe that a regulatory body would be bound by a rigid mathematical calculation of weighted average cost of capital based upon total capitalization, for purposes of setting a rate of return on rate base. In 1975 and 1976, the Commission set rates for Appalachian based upon an 8.73% rate of return to be applied to a 13-month average rate base for West Virginia. Not too many decades ago, in an era having low inflation, rate of return was not a major item to be litigated in ratemaking. It was recognized then that 6% was a fair, just and reasonable rate of return to be allowed by regulatory bodies. Utilities planned their growth, financing, and operations accordingly. During this period, utilities were able to grow at a reasonable pace to meet their public service obligations and

prosper. Within the past quarter of century, however, inflation and dislocations in the economy, due to such things as widespread and substantial governmental deficit spending, have increased the cost of capital, which, in turn, has affected a steady increase in rates of return allowed on rate base in ratemaking. We trust that there is a point in the not too distant future when the government and the governed will realize spiralling inflation must be stopped and take steps to do so, so that utilities will grow and serve the public within the limits of a non-increasing rate of return on rate base.

Looking first at the cost of capital criteria for determining rate of return, we find that Appalachian seeks a rate of return on year-end rate base in the range of from 9.65% to 10.1%. Appalachian would translate cost of capital expressed in percentage of total capitalization to rate of return on rate base with no other considerations. Moreover, Appalachian would have us believe that the calculated weighted cost of capital is a fixed and proper rate of return, regardless of the rate base to which it is applied. This is not true when one considers the many variances possible in arriving at an allowable rate base. Thus, both the cost of capital and the methodology employed in arriving at rate base must be considered before a fair rate of return can be determined. The Staff cost of capital witness followed the same basic error of believing in strict translation of cost capital into rate of return on rate base. On this basis staff recommended a 9.42% rate of return based upon evidence of cost of capital at December 31, 1975, of from 8.75% to 9.16%, and cost of capital estimated at December 31, 1976, to range from 9.17% to 9.67%.

An equally important consideration in determining rate of return is the necessity for higher earnings. If higher earnings are needed for improvident or excessively accelerated expansion or for excessive return to the common equity owners, the requested rate of return would be too high.

Here, however, Appalachian carried its burden of showing a need for rate of return higher than the 8.73% previously allowed, albeit not at the levels requested. Appalachian presented evidence that its senior securities and commercial paper had been downgraded to be at the lowest rating of all of the major electric utilities in the country. It argues that its debt coverage is dangerously low, so as to limit its ability to finance growth needed for its generating and transmission capacity. Appalachian argues that it needs higher rates to restore to a normal construction level its project 1300 megawatt generating unit partially completed at its site in New Haven, Mason County, West Virginia. In Case No. 8401, by order issued April 29, 1976, this Commission certificated Appalachian's 765-kV high voltage transmission line to run from Culloden in Cabell County to Wyoming County, West Virginia, while recognizing that Appalachian contended that it needed rate relief in Case No. 8182 in order to construct the $72 million project. Appalachian estimates its 1976-1980 construction program will require up to $1.3 billion, which would average $260 million per year. A portion of this financial requirement will be generated internally, with the balance raised from investors. In either case, Appalachian will require an improvement in earnings to be able to continue a reasonable growth to satisfy the electricity demands of an energy-short public.

There are several considerations, however, which militate against allowing a rate of return as high as is recommended by Staff or by Appalachian. First, the Commission has been liberal in its allowance of adjustments to fuel expense and other expenses for the second-tier rates. Second, we have permitted a measure of CWIP in rate base. Third, as discussed below, we are allowing a partial normalization of federal income taxes in order to improve the quality of earnings and to encourage growth of plant. Fourth, we have grave reservations about whether or not

West Virginia is paying its proper share of total costs vis-a-vis sales by Appalachian subject to other regulatory bodies as discussed below. Finally, the customers of Appalachian in West Virginia are not able to give it *carte blanche* for unlimited rate increases which cannot be absorbed by their limited incomes.

In the light of all of these considerations and the evidence, the Commission finds in its judgment that the allowable rate of return on rate base for Appalachian in this case is 9.35% for West Virginia.

It is hoped that Appalachian will be able to reduce unnecessary or unreasonable costs—such as (1) its cost of coal purchased from its affiliates and (2) other Account 501 fuel costs—in order to earn *more* than 9.35% on total capitalization. The actual results of future fiscal periods will reflect the good or bad results of management decisions, increased sales volumes, and efficiencies that will come with additional modern generating units and high voltage transmission systems. By keeping rates at levels which will recover no more than the lowest possible *reasonable* level of test year costs, we regulate in a balanced way to induce management to search for cost reductions, prudent growth, and greater efficiencies in operations.

8. Federal Income Tax Expense

As a general principle, a public utility must be allowed rates high enough to generate revenues sufficient for it to pay its federal income tax liability. It seems only just that public utilities pay their fair share of the cost of our federal government. Moreover, when a Company seeks and secures a rate increase, it would usually be expected that its greater revenues would result in higher earnings and, therefore, a higher income tax liability. However, under current federal income tax laws, this is not always the fact.

In Appalachian's situation it can generate millions of dollars of earnings which are subject to very little or no income tax liability because of Congressional modification of the tax laws which have accomplished the following:

(1) Profitable members of a public utility holding company system can enjoy tax savings due to the election by all of the members of the system to file a consolidated income tax return through their parent corporation, under Section 1501 of the Internal Revenue Code.

(2) Public utilities are allowed tax credits reducing their federal income tax liability in varying percentages of investments in public utility property, depending upon (a) the dates of installation, (b) the nature of the property, such as pollution control facilities, (c) the mode of rate regulation by regulatory bodies having jurisdiction and, (d) timely accounting and tax elections by the regulated utilities, all under Sections 38, 46 through 50 of the Internal Revenue Code.

(3) Public utilities are allowed accelerated depreciation and amortization deductions from gross taxable income at higher levels than booked under the straight line depreciation method used for certain depreciation expenses for non-tax purposes, depending upon (a) the dates portions of the property are placed into service with reference to pre-1970, post-1969 and facilities in operation before 1976 requiring pollution control additions, (b) timely accounting and tax elections by the regulated utilities and (c) the manner of rate regulation by pertinent regulatory bodies having jurisdiction, under Sections 167 and 169 of the Internal Revenue Code.

The history of the underlying tax statutes reveals the attempts of Congress to reconcile the interplay of two principles. First, there was the Congressional attempt to stimulate the economy by tax concessions to businesses to

encourage growth of tangible capital assets. Second, there was Congressional vacillation from time to time between attempts to limit and attempts to assure the benefits of tax concessions to public utility business enterprises. In so doing some states believe that these Federal tax laws threaten to cause an incursion by the Federal Internal Revenue Service in the ratemaking processes which are the jurisdiction of State regulatory bodies. The potential conflict between the Federal IRS and certain State regulatory bodies is materializing in California, where that State is reducing utility rates in a way that, under Section 46(f) of the Federal income tax law, certain California utilities may lose their tax credits and earlier tax savings and be assessed huge amounts of additional taxes.

Our West Virginia Public Service Commission need not and will not involve itself in this case in the type of controversy that is brewing in California. Appalachian has demonstrated that it needs substantial moneys from (1) earnings, (2) tax savings or deferrals, and (3) the financial market to be able to invest in new or expanded generating, transmission, and other facilities to be able to render adequate service to its broad market. Moreover, all parties to this proceeding concede that this Commission can grant, withhold, or modify its allowable Federal Income Tax expense and accruals to be used in the cost of service and rate base for ratemaking purposes in relation to normalization, averaging, or other methods of ratemaking, so long as this Commission does not "plainly contravene" the statutory scheme and the precise limitations of the Internal Revenue Code where Congress has failed to give rate regulatory bodies a formula to follow. *F.P.C.* v. *United Gas Pipeline Co.*, 386 US 237, 87 SCt 1003, 68 PUR3d 321.

Appalachian has elected to participate in the benefits of consolidated tax savings and investment tax credits and now seeks to switch from "flow through" to "normalization" accounting and ratemaking for certain, but not all, of the

tax benefits that result from adopting available tax depreciation methods which provide greater early year tax deductions and, therefore, less current income tax liability than would be derived from using booked straight line depreciation for tax purposes.

The Commission's discretion in determining an allowance for federal income tax expense in ratemaking must start with the fact that a projection of test year pro forma revenues, expenses and rate base cannot be an exact forecast of the immediate future after a rate adjustment is allowed. This is particularly true with respect to Federal Income Tax expense, because too many variables are involved, some of which are within and some outside of the control of the utility. For example, tax credit rates are changed by Congress; the taxpayer can switch his options to minimize his tax over several tax periods; qualified public utility properties can go into service at accelerated or delayed dates at management election; carryback and carryover of unused tax credits can distort the matching periods of expenses and revenues, and tax audits by the Internal Revenue Service can substantially change a utility's actual tax liability several years after the tax period.

As we stated in Case No. 8000, Columbia Gas of West Virginia, Inc., order issued June 16, 1976:

> "An informed judgment to determine an allowable federal income tax component in a cost of service for ratemaking purposes is a substantially different thing than calculating the actual taxes to be paid by a utility in its annual tax return. When regulatory bodies and reviewing courts say that only 'actual taxes paid' should be allowed in the cost of service for ratemaking purposes, they are enunciating a broad, general principle, which has certain limitations which must be fully understood when the principle is applied."

We start now with our findings on each subsidiary Federal income tax issue to be sure that they are based on rational criteria.

A. Consolidated Tax Savings

Appalachian agrees that tax savings derived from filing a consolidated tax return by its parent, American Electric Power, Inc., should be *shared fairly* with Appalachian's West Virginia customers. Appalachian contends, however, that the portion of tax savings due to the losses of the parent corporation should not be used in the formula for determining consolidated tax savings. The net effect of the Company position would reduce the average of consolidated tax savings percentages as compared with the results of separate tax filings, so as to reduce the consolidated tax savings and thereby increased the Federal income tax expense to be recovered as part of the total cost of service used in ratemaking. Appalachian would impute to itself the portion of its parent corporation's tax loss benefit derived by the percentage which Appalachian's taxable net income bears to the total taxable net income of the taxable net income companies. Staff, on the other hand, would calculate consolidated tax savings on the basis of including parent company losses with the other elements that create a consolidated tax savings and would apply a percentage reduction for consolidated tax savings to pro forma taxable income. Appalachian contends the consolidated tax savings should not be increased as incrementalized to pro forma taxable income and that the test year tax savings should be $664,371, instead of the $4,100,837 tax savings allocated to West Virginia.

Staff has followed long-standing Commission precedents in its method of estimated consolidated income tax savings, which have a rational basis. The Company method is not shown by the record to have any greater validity. Because

of the variables involved and the inherent imprecision in projecting a test year pro forma income tax allowance, the staff evidence based on historical facts of consolidated tax savings over a three-year averaging period (1971-1973) is found to be reasonable.

B. Investment Tax Credits (Job Development Credit)

The calculation of investment tax credits for a public utility's Federal income tax return is a most complicated task. Appalachian has been "flowing through" tax savings from the investment tax credits, which were 3% in 1962-1968, 4% in 1971-1974, and 10% starting in 1975. The tax credits are derived by multiplying these percentages times qualified investments in public utility facilities placed in service in the appropriate years and increased, if elected, by 3-year carryback and 7-year carryover of unused tax credits. There are other complexities; such as, "transitional rules" for the period between January 21, 1975 and January 1, 1981; limitations on the magnitude of the tax credits, and variable percentages of aggregate qualified investments of varying service lives in tax years 1975-1980. Suffice it to say that projecting an estimate of investment tax credits for the immediate future, as represented by a pro forma test year, which will approximate the *actual* investment tax credits to be realized is purely a matter of regulatory judgment and discretion. In these circumstances, the averaging method of projecting an estimate of the tax credits is a conservative way of determining a fair reduction in allowable Federal income tax expense.

Appalachian attacks the Staff method of using a 5-year average, rather than a 3-year average, without a maximum 90% limitation. Appalachian claims that the 5-year period includes qualified investments arising from its additions at its Amos plant, and that this unreasonably inflates the tax credit base used in the averages. The Company points

to its investment tax credits (unaudited by IRS) of $2.6 million in 1974, $4.4 million in 1975, and estimated $8.3 million in 1976, for a 3-year average of $6.7 million, instead of the $11.2 million proposed by Staff.

The record indicates Appalachian's qualified investments for tax credit purposes will increase substantially over the next five years. Moreover, its experience over the last three years indicates a steady growth of investment from a low point in 1974. The Staff method is found to be reasonable and is adopted by the Commission in calculating federal income tax expense.

C. "Normalization" of Tax Benefits Due to Accelerated Depreciation and Amortization as Tax Deductions and Investment Tax Credits

In the past Appalachian has used the "flow through" method of financial and ratemaking accounting with regard to income tax benefits attributable to (1) liberalized depreciation, (2) class life asset depreciation range, (3) asset depreciation range repair allowances and (4) investment tax credits.

Appalachian now wants to shift from "flow through" to "normalization" accounting in order to justify higher rates to its West Virginia customers. Appalachian argues that the benefits of "normalization" will outweigh the burdens.

The concepts of "flow through" and "normalization" accounting are understood to be as follows:

(1) "Flow through" accounting is used where the utility elects to use certain statutory tax-saving or tax-deferring provisions for (a) accelerated depreciation or amortization as deductions from gross taxable income, or (b) tax credits, and then the utility calculates Federal income tax expense for ratemaking purposes on the same basis. "Flow through" accounting in test year ratemaking is sometimes

broadly characterized as a method to allow recovery in rates of "actual taxes paid".

(2) "Normalization" accounting is used where (a) the utility employs straight line depreciation for tax purposes in ratemaking, even though it actually uses an accelerated depreciation or amortization for calculating taxes paid to the Internal Revenue Service and where (b) the benefits attributable to the investment tax credit are distributed over the life of the qualified asset, rather than in the year the tax credit is received.

Appalachian urges approval of its partial shift to "normalization", because it sees the resultant increase in cash flow as a means of improving its debt service coverage and ease its outside financing, as well as a means of increasing the amount of internally generated funds needed for construction. Appalachian argues that normalization is a method of accrual accounting which better matches revenues and expenses for services rendered. It would use an accumulated deferred income tax reserve to reflect the excess of normalized Federal income tax over that actually paid to the IRS during the early years of property life and would deduct the reserve from rate base or give an equivalent portion of the rate base a zero rate of return.

The Staff of the Commission presented its initial evidence on the basis of "flow through" and, subsequently modified its position to favor normalization of all tax benefits, except investment tax credit. At a Staff-recommended 9.42% rate of return level, the cost of service using normalization would be $5,215,951 higher than that obtained from a flow-through calculation. We decline to follow either the Staff or the Company's recommendations. We will adhere to a "flow-through" of tax benefits from liberalized depreciation, class life asset depreciation range (ADR) and ADR repair allowances, but we will allow normalization of investment tax credit benefits.

We reject normalization of tax benefits derived from using optional deductions from gross taxable income, because of our inability to fairly predict the tax effects of future elections by the taxpayer. In this very case, Appalachian changed its position and elected *not* to take accelerated amortization on pollution control facilities which were placed in service in 1975, under § 169 of the Internal Revenue Code because it wanted to minimize the payment of a 10% minimum tax on certain tax preference items and to increase its investment tax credit carryforward and increase its taxable income "without any change in the regular taxes payable".

On the other hand, we will permit the Company to "normalize" its investment tax credit benefits for ratemaking purposes in the unique circumstances of this case. Appalachian has elected *not* to use the option available under Section 46(d) of the Internal Revenue Code which allows an investment tax credit for qualified progress expenditures before the property is placed into service. Since we do not allow all Construction Work In Progress (CWIP) in rate base, we would be reluctant to allow normalization of investment tax credit benefits on property not yet placed in service.

Section 46(f) of the Internal Revenue Code provides the general statutory rule that no investment tax credit will be allowed to a public utility, *if a rate regulatory body* (1) reduces the utility-taxpayer's cost of service for ratemaking purposes by reason of any portion of the investment tax credit, or (2) reduces the utility-taxpayer's rate base to which the rate of return is applied for ratemaking purposes by any portion of the investment tax credit. The tax statute limits this general rule in various ways and without timely utility-taxpayer elections to the IRS. Obviously, the intent of this Federal statute is to encroach on the freedom and jurisdiction of State regulatory bodies

in ratemaking so as to aid public utilities to generate internally or to finance funds for construction of public utility facilities.

The West Virginia Public Service Commission need not raise the question under the 9th and 10th Amendment to the Constitution of the United States of whether Federal tax laws can control or impair a State's rights to regulate intrastate utility rates. We need not do so here because we recognize Appalachian's need for additional cash flow to be able to construct substantial additional facilities to continue to render adequate service to the public. The overall intent of the maze of shifting tax laws is that there should be some measure of *fair sharing* of tax benefits between utility taxpayers having growth problems and the ratepayers who also have limited financial means. By permitting Appalachian to adopt normalization of investment tax credit in this case, the Commission can still regulate Appalachian's level of Federal income tax expense used in ratemaking by an averaging technique such as the 5-year average of qualified investment used by the Staff and approved for this case.

We recognize that it is difficult to predict the tax benefits of future elections as to investment tax credits, but since this will be a direct reduction of taxes in each fiscal year it is more susceptible of fair regulation by averaging than would be the Sections 167 and 169 I.R.C. tax benefits by savings or deferral through "normalization" accounting and ratemaking. We must insist, however, that the rate base be reduced by any accumulated deferred reserve resulting from normalization and the deferred credits should be amortized over the life of the public utility property involved.

Following the methods approved above for calculating a test year, pro forma, Federal income tax expense to be used in ratemaking, we find that $4,573,249 is a fair, just and reasonable amount to be included in total cost of service based upon a 9.35% rate of return on a West Virginia rate base of $488,550,995 for the first-tier rates effective August 28, 1975 through April 30, 1976. Furthermore, we find that $4,596,410 is a fair, just and reasonable amount to be included in total cost of service based upon a 9.35% rate of return on a West Virginia rate base of $488,976,907. For the second-tier rates effective on and after May 1, 1976, see Appendices B and C attached hereto.

9. Jurisdictional Cost Apportionment

The second step in the ratemaking process, after determining the aggregate test year, pro forma total cost of service or revenue requirements, is to decide how much of the total is the fair responsibility of West Virginia *vis a vis* Appalachian's other markets in Virginia regulated by the Virginia State Corporation Commission and Appalachian's markets regulated by the Federal Power Commission. We approach this task with caution, not only because the process of jurisdictional cost apportionment is complex and ephemeral, but also because it should not put the customers in any rate jurisdiction or the Company itself at an undue or unreasonable disadvantage. In short, we must be fair and balanced in our determination of this issue.

Before considering subsidiary issues, certain factual data should be set forth as a point of reference that is not lost in a welter of statistical evidence. Upon the premise that the regulatory bodies of West Virginia, Virginia, and

the Federal Power Commission set rates on the basis of costs and each has to apportion total costs for ratemaking purposes in their respective jurisdictions, we note Appalachian's sales volumes, and unit revenues per kilowatt-hour sold over the period 1971 through 1976.

Except for unavailable interchange-out sales revenues to non-affiliates on billing units of 573,872 megawatt-hours in 1971 and 623,347 megawatt-hours in 1976, Appalachian's gross revenues increased from $238,924,000 in 1971 to $677,499,000 in 1976. Dividing pertinent kilowatt-hours sold of 19,552,038,000 in 1971 and 31,853,031,000 in 1976 into these revenues we find Appalachian's *aggregate* unit revenues increased from 1.22¢ per kilowatt hour in 1971, to 2.12¢ per kilowatt-hour in 1976, on said sales volumes. The underlying unit revenues by rate jurisdiction is shown on Appendix D hereto and as follows:

	1971	
1.22¢/Kwh on Aggregate Sales of 19,552,038,000 Kwhs	on (W.Va.) sales of 7,407,817,000 Kwhs	1.34¢/Kwh
	on (Va.) sales of 6,216,874,000 Kwhs	1.44¢/Kwh
	on (FPC) sales for resale of 3,786,979,000 Kwhs	.92¢/Kwh
	on (FPC) sales to affiliates of interchange-out of 2,140,368,000 Kwhs	.70¢/Kwh

	1976	
2.12¢/Kwh on Aggregate Sales of 31,853,031,000 Kwhs	on (W.Va.) sales of 8,745,946,000 Kwhs	2.64¢/Kwh
	on (Va.) sales of 7,875,839,000 Kwhs	2.69¢/Kwh
	on (FPC) sales for resale of 9,159,250,000 Kwhs	1.71¢/Kwh
	on (FPC) sales to affiliates of interchange-out of 5,961,996,000 Kwhs	1.30¢/Kwh

A. *Energy Cost Apportionment*

Several observations can be made from the foregoing facts, and Appendix D hereto, which also shows the detail of the intervening years between 1971 and 1976. First, for those who are "marginal cost" or "long run incremental cost" devotees, using 1971 as a base, Appalachian's growth in energy sales is shown to be predominately the responsibility of its FPC jurisdictional customers who purchased 9,243,374,000 Kwhs (or 75.9%) of Appalachian's incremental growth of energy sales 1976 over 1971 of 12,340,468,000 Kwhs. On a comprable [sic] basis, West Virginia realized a growth of 1,338,129,000 Kwhs (or 18.1%) and Virginia experienced an incremental increase in sales of 1,658,965,000 Kwhs (or 26.7%).

Yet, even with the substantial increase in energy requirements of the interstate market, Appalachian increased its unit revenue yield in 1976 over 1971 only by .60 (Interchange-out to affiliates) and .79 (Sales for resale) cent per kilowatt-hour for the FPC jurisdiction, which required the largest growth of energy requirements. In contrast, Appalachian exacted an incremental unit revenue increase of 1.30¢/Kwh for West Virginia and 1.25¢/Kwh for Virginia.

This Commission fully recognizes that the aggregate of sales under FPC jurisdiction may cost less per unit than does the aggregate of sales in the two State jurisdictions. This is because certain of the sales under FPC rate schedules may justify a lower demand cost responsibility than do the State sales and for other reasons, such as that a "wheeling" power service has little or no *energy* cost responsibility. However, the major cost increase experienced by Appalachian during the period 1971 through 1976, has been the hyper-inflationary jump in fuel costs. With this in mind, the substantially lower unit revenue increases for *FPC* jurisdictional sales as compared with *State* jurisdictional sales are suspect. It will only be with a fully

distributed jurisdictional cost apportionment study that regulatory bodies can act to avoid the possibility that West Virginia and Virginia are subsidizing Appalachian's interstate sales.

Both the Staff and Appalachian credited interchange-out revenues to total cost of service prior to the apportionment of costs by segregation or allocation factors based upon demand and energy components. Therefore, we have no way to test whether or not such FPC rates are too low against the backdrop of escalating fuel costs. We do know, however, that the use of the "revenue-credit-to-cost of service" method sponsored by Appalachian would assign cost recovery deficiency in such sales to West Virginia. In view of the lack of evidence on this issue involving interchange-out sales, we can do no more than accept the revenue-credit method used by Appalachian and the Staff for interchange-out sales. However, since the energy growth responsibility is shown to have been that of the FPC jurisdiction, we believe our concession in this regard is in favor of the Company and counterbalances other determinations in this order which Appalachian might consider as less than liberal to the utility.

In Case No. 8401, order issued April 29, 1976, we adverted to these same problems, and those pertaining to the lack of accurate and complete demand data, for use in cost apportionment. We noted there that:

> "Appalachian has embarked on a load research program to determine by sampling a more representative assignment of cost responsibility for its rendition of service."

Although this is more appropriate to cost apportionments to classes of service, rather than to jurisdiction, we are putting Appalachian on notice by this order that we expect Appalachian to come in with a full cost apportionment study *with measured data* as far as possible in its next rate case.

This Commission is charged with the responsibility of protecting West Virginia customers from the burden of any undue or unreasonable subsidization of other markets. We turn now to the issue pertinent to the *demand* responsibilities for assigning costs.

B. *Demand Cost Apportionment*

Unlike energy sales, all of the peak hourly demands (KW) of jurisdictions and classes of service are *not* measured. Those not measured are derived by formula. Nevertheless, the Company attempts to assign *demand* cost responsibility on the basis of peak hour demand, even though there is very little measured data of peak demands. Appalachian (1) uses demand allocation formulas that impute demands to classes of service of jurisdictions or else (2) it credits revenues against production costs before demand or energy allocations are begun. The latter method creates the fiction that such revenues cover a fair portion of all of the costs of such service. In the opinion of this Commission, unless such sales treated by the "revenue credit" method are relatively insignificant, the crediting of such revenues against total costs prior to cost apportionment is tantamount to assuming the fact in issue or "begging the question" of the fairness of cost apportionments within the total. Cf. Case No. 8000, *Columbia Gas of West Virginia, Inc.*, order issued May 14, 1975.

In its evidence, Staff included the measured peak hourly demands of Appalachian's short-term, limited term and unit power sales in megawatts in the development of the Staff's demand related allocation factors. Also, Staff included kilowatt hours of sales from these customer classes in the development of energy related allocation. These sales are regulated by the Federal Power Commission. Appalachian characterizes them as "non-firm" sales, even though they are "firm" to the extend [sic] of their contract

terms and have high priority in the event of future power shortages.

Appalachian opposes the staff approach on this issue, even though it had used the same method in its last major rate case, No. 7083, decided by this Commission. It does so on the ground that since neither Appalachian nor its parent plans or constructs facilities for short term, limited term or unit power sales that these classes of customers are not responsible for a fair portion of the costs of the system installed and operated to render all service.

The record indicates that even if it is true that Appalachian's system is not planned for these sales, there is no question that its system was *used* for these sales on the peak hour and in energy or commodity sales. The Commission finds that costs should be apportioned after considering the percentage effects of the *actual use* of facilities during the test year on the peak hour, as well as throughout the test year. In an integrated electric system having periodic spurts of growth, new capacity is made available prior to the time needed. The members of the system, as well as outside purchasers of power for resale know that there will be excess power available by design or by the principle of diversity, until growth stops at some unknown point in the future. When such customers contract for service, other than (1) purely emergency energy service, (2) interruptible economy energy service or (3) surplus or dump energy service, they pay a rate which includes a capacity or demand charge. If any service has a demand cost element underlying the capacity charge in its rate, that service should be tested to be sure that it bears a *fair* portion of the demand costs. Crediting such revenues against costs by-passes this issue. It would permit the Company to avoid the determination of the question of "How much is fair?".

What should not be lost sight of is the use that is made of a demand allocation factor. For example, staff applies the demand-allocation factor to most transmission operation and maintenance expenses. These expenses are for the benefit of the short-term, limited-term and unit-power customers, as well as other customers of Appalachian. All of these customers should bear a portion of the capacity costs of the facilities used to serve them.

We find that the staff method of jurisdictional cost apportionment is just and reasonable.

10. *Class of Service Cost Apportionment*

The third step in the ratemaking process is to assign the West Virginia costs to the classes of service within West Virginia which are subject to the rate jurisdiction of this Commission. This step is a necessary prelude to the final step or ultimate rate design process in ratemaking.

Classes of service within West Virginia include residential, commercial, industrial and others (sales for resale [FPC], street lighting, and sales to public authorities).

The costs of service for these classes should also involve cost apportionments if there is to be a change in rate design from historical differentials. Even if there is no change in rate design, the Commission should periodically test the propriety of the differences in rates as among classes of service. "Class of service" cost apportionment is just as complex and ephemeral as is "jurisdictional" cost apportionment.

Here, too, those who are "marginal cost" or "long-run incremental cost" devotees tend to jump to the conclusion that industry is responsible for Appalachian's growth and that the residential market is subsidizing the industrial market.

Our point of reference is the growth of sales volumes and revenues by classes of service over the period 1971 through 1976. See Appendix E hereto.

An interesting observation from this factual data is that, using 1971 as a base, the incremental growth of Appalachian's 1976 sales in West Virginia amounting to an aggregate of 1,354,505,189 kilowatt-hours is attributable as follows to the classes of service:

	KWHs	%
Residential	884,396,695	65.7
Commercial	379,778,318	28.0
Industrial	67,570,242	5.0
Others (Sales for resale [FPC], street lighting and sales to public authorities)	22,759,934	1.3
Total	1,354,505,189	100.0

In the face of these growth patterns of energy sales, realization of unit revenues by classes are as follows:

	Cents Per Kilowatt-Hour		1976 Over 1971
	1971	1976	%
Residential	2.09	3.22	54
Commercial	1.91	3.18	66
Industrial	.94	2.10	123
Others (Sales for resale [FPC], street lighting and sales to public authorities)	1.76	2.39	36
Total	1.38	2.63	91

These comparisons show that the *industrial* market grew by only a 5% increment of total market growth, while paying Appalachian a 123% incremental increase in unit revenues. On the other hand, the *residential* market grew by a 65.7% increment of the total growth, while providing Appalachian a 54% incremental increase in unit revenues. This is *not* to say that unit revenue growth by classes of service should match or even closely approximate growth in kilowatt-hours of sales. However, the great disparity shown is indicative that cost apportionment by classes of

service is required to test the fairness of rates as among classes of service in West Virginia. This is particularly true, since the accelerated fuel costs is [sic] such a large part of Appalachian's cost of service.

Neither Appalachian nor the Staff submitted cost apportionment studies by classes of service. In our order issued April 29, 1976, in Case No. 8401, we noted that Appalachian contended it was not possible to allocate peak demand among classes of customers, since only a small part of the component parts of that peak hourly demand among various classes of customers is measured. Appalachian has been put on notice for more than two years, that it must prepare such a study. It is our understanding that such a study by use of a sampling technique is soon due. A fully distributed cost apportionment study by classes of service will be required.

11. *Rate Level and Rate Design*

The final step in the ratemaking process is to set rates, tolls or charges for service to each customer class and for each demand and usage block at rate levels which are no more than the specific service is reasonably worth to the various customers "considering the cost thereof". Code 24-2-2. These rates and charges must be just, reasonable and fair to all segments of the public involved. Code 24-2-3. The public involved includes the public served and the public servant. The public served includes classes of customers, as well as customers within each class that require very little electricity or extremely large amounts of power. These requirements may and often do vary from hour-to-hour, from day-to-day, from month-to-month, from season-to-season and from year-to-year. Since the metering for these peak and volume fluctuations over various periods of time, and the compilations of the resulting measurements would be extensive and expensive, various compromise rate

forms have been designed and used to achieve rate fairness. One of these rate designs is the declining block form of energy rates as a simplification of cost related rates.

Currently, there is a lack of understanding of the declining block rate form leading to debatable conclusions, which, if put into effect, may adversely affect the well-being of every element of the public. There are those in influential positions who say that electric rates should not have a lower tail block rate for the large users. They contend that this is "promotional" and provides high usage customers with an unfair preference over low use customers. Moreover, the argument goes further to characterize declining block rates as being contrary to a conservation of energy policy and a burden on the poor.

The Parable of Milk

Often, both experts and newcomers in the energy-rate debate deal with the pet phrases and esoteric vocabulary of the controversy without a full understanding of the limits and ambivalence of the terms and pertinent concepts. Thus, for a better understanding of declining block rates and their underlying costs, we believe that an explanation by way of analogy in terms of the sale of milk would be helpful.

Our parable involves two extremely poor families—(1) an elderly widow on social security who lives alone, and (2) a husband and wife with two children living on welfare.

The *elderly widow* buys a quart of milk a week at 50 cents a quart, from which she can drink 5 glasses of milk each week at 10 cents per glass. She cannot buy more than a quart of milk a week because she does not have the money. Even if she did have an extra 50 cents, she would not buy a second quart or a half gallon of milk because it might spoil in her tiny refrigerator.

The *welfare husband* buys a gallon of milk a week at $1.50 per gallon, from which he, his wife and their two little

children can drink 20 glasses of milk. Thus, each of the four persons can drink 5 glasses of milk each week at 7½ cents per glass.

Looking at these two sales *from the point of view of the supplier,* it costs the dairy more to supply a quart of milk than it does to supply a gallon. The dairy pays more per carton to buy a few quart cartons, fill them, and handle them, than it does for it to buy the more popular gallon cartons, fill and handle them. The dairy may have less of a profit margin on each six ounces of milk sold by the *quart,* than it does on each six ounces of milk sold by the *gallon.*

Although the analogy is not perfect, these prices could be stated in a "declining block" price form, rather than a "per carton" price form, to be 10 cents per glass for the first 5 glasses of milk and 6.67 cents per glass for the tail block of 15 glasses of milk.

From the point of view of the two poor milk customers, the widow cannot justly complain that she is being discriminated against because her milk purchased by the quart costs her 10 cents per glass rather than 7½ cents per glass when purchased by the gallon. If the welfare husband was forced to pay 10 cents, instead of 7½ cents per glass, such would not encourage conservation of milk.

If government stepped in and ordered the dairy to reduce the price of a quart of milk from 50 cents to 38 cents, so that the widow could get milk at 7½ cents per glass, it is possible that the dairy could not sell milk in quarts at that price without suffering an out-of-pocket loss. It would not be just for the dairy to raise the price of a gallon of milk to the welfare husband, so as to make up for the loss from the sale to the widow at below cost.

Application of the Parable to Electricity

Any arbitrary, blanket condemnation of the declining block form of electric rates can very easily create the same

kind of potential injustice as is suggested in the milk parable. Without valid studies of the cost of supply power at various voltages, demands and amounts of energy, flattening or inverting the block form for electric rates can cause the utility to sell power at a substantial loss or require other customers to pay an inordinate electric rate to subsidize the low user. Although the poor person is more often than not a low user of power this is not always the case. Moreover, there are many more electric customers in West Virginia who are *not* poor and who are also low users of electricity.

In the discouragement of large uses of power by high rates and abruptly changing rate forms, such discouragement does not distinguish between the prevention of ***good*** uses of electricity and ***wasteful*** uses. Morover, if the large users of electricity are providing the utility with substantial amounts of revenues to cover the utility's costs and profit margin, any forced reduction in use in substantial amounts by penalty pricing may either cause the utility to shift the cost burden to other customers or absorb the loss itself and thus weaken its financial condition and its ability to serve.

By this discussion this Commission does ***not*** imply that electric rates should not be flattened or changed in any way from the declining block rate form. We merely caution that it should not be done abruptly or without valid supporting cost apportionment studies.

We turn now to the rate design issues posed for decision in this proceeding.

Residential Rate Design

Appalachian proposes to eliminate its lower water heater service rate for residential (R.S.) customers, and after eliminating or phasing out its Church Service (C.S.), Electric Heating-General (E.H.G.), School Service (S.S.),

Capacity Power (C.P.) and Large Power (L.P.) services, it would spread the rate increase by an across-the-board percentage.

Appalachian Research and Defense Fund, Inc., et al, ("Low Income Intervenors") urge the Commission to grant little or no increase in the residential rate, and an increase of .21¢ per Kwh for the commercial and industrial customers who purchase under the Commercial-Industrial Power (C.I.P.), Large Capacity Power (L.C.P.), Transmission Power (T.P.) and High Load Factor Power (H.L.P.). The Low Income Intervenors urge a departure from the declining block rate structure to an inverted block rate structure of 2¢ per Kwh for all usage above 200 Kwh and 4¢ per Kwh for all usage above 200 Kwh per month, *but* with *credits* given for off-peak usage for electric hot water and/or electric space heating. In addition, they recommend "the reduction of 'submarginal' rates", which is interpreted by the Commission to mean that any rate preference now being given to the low use or initial block rates should be further reduced. The theory underlying this proposed rate innovation and attack on the declining block rate form is that of "marginal cost" or "long run incremental cost". As to "peak load" or "time of day" pricing, the Low Income Intervenors do *not* recommend that residential customers be put on that type of metering or rate form at the present time, because the cost of necessary metering would be too high.

Protestant, Council of Senior Citizens, contends that Appalachian's tail blocks are too low and *assumes* that the growth in demand causing Appalachian to grow in demand and energy supply is due to the requirements of the industrial and commercial markets.

FMC Corporation, ACF Industries, Inc., American National Rubber Co., Chemetron Corporation, Huntington Alloys, Inc., Hondaille Industries, Inc., and Owens-Illinois,

Inc., ("Industrial Intervenors") oppose the "marginal cost" theories and rate design proposals of the Low Income Intervenors. They point to the danger of loss of industry to other States by excessive rates to West Virginia industry. They discuss weaknesses in the theory and factual background of the "marginal cost" arguments made by the Low Income Intervenors.

The Staff of the Commission notes that the record is bare of a fully distributed cost of service study by customer class, but that such a study (requested by the Commission in April of 1975) was expected soon. In this posture, the Staff opposes the elimination of certain rate schedules and would spread any revenue deficiency over all classes of service on a percentage basis.

The Commission finds that in the absence of a cost apportionment study or studies, it will generally adhere to the historical rate form, with certain minor discretionary modifications, and will deny the proposed changes in rate form made by Appalachian and urged by the Low Income Intervenors. We do this without prejudice to our future actions which may change the historical rate forms used by Appalachian on the basis of valid cost apportionments and other considerations.

On the present record we have no way of knowing whether the discount given to residential water heating customers or electric heating-general customers is fair or not. It could very well be that a cost apportionment study would indicate that the large users in the residential class of service are already contributing more through the low blocks of their rates towards the costs of serving them than is justified. The opposite could also be true.

We do know, however, that the residential market in West Virginia is more responsible for Appalachian's growth over the period 1971-1976 than is the industrial market, although it appears that the major cause of growth

is due to the demands for electricity outside of West Virginia. Thus, if we were to be influenced by the "marginal cost" or "long run incremental cost" theorists, we would be led to the conclusion that the residential market growth is more responsible for Appalachian's growth of facilities in a hyper-inflationary age, than is industry.

As to the Low Income Intervenors' recommendation that the block rate form be inverted, not only is the record void of probative evidence to quantify such a rate form on a just, reasonable and fair basis among the various classes of customers—even with a preferential bias to the residential class, but also the argument of the Low Income Intervenors is weakened by their recommendation of a *credit* (of unknown magnitude) for water and space heating customers.

We do recognize that the debate is not ended and that the poor customers do have a need for every consideration. Therefore, in an effort to move towards a gradual flattening of the declining block rate form, we will design residential rates herein which will spread the rate increase *after skipping the first usage block* of the R.S. rate schedule. We do not do this arbitrarily, but act after analysis of the effect of Appalachian's informational filing pursuant to ordering Paragraph 4 of our order issued January 31, 1975, in Case No. 7083, and the facts of record in this case.

The "end results" of this and other rate design issues determined herein are set forth in Appendix F to this order.

Abrupt Elimination of Industrial and Commercial Rate Schedules

In Appalachian's proposed W.Va. P.S.C. Tariff No. 3, in effect tentatively since August 28, 1975, in addition to its abrupt elimination of the water heater service for residential customers discussed above and reinstated herein, Appalachian deleted its Combined Light & Power (C.L.P.), Capacity Power (C.P.), and Large Power (L.P.) rate schedules previously available to certain of its industrial and commercial customers.

The Commission has been informed that Appalachian had no commercial customers purchasing under its C.L.P. rate schedule. We have no objection and approve the deletion of this portion of the tariff as superfluous. The C.P. and L.P. rate schedules were previously available to certain customers. We find that Appalachian failed in its burden of proof to justify the deletion of these services, because it presented no cost data to support its managerial decision and other considerations discussed below.

L.P. Rate Schedule

The Large Power service rate was available to customers who contracted to pay for a definite, large amount of electrical capacity in excess of 50 KVA in multiples of 25 KVA. The rate was composed of a demand charge and a declining block energy charge, with a minimum monthly charge also composed of demand and energy components. The record does not reflect which customers were served under this rate schedule. After the L.P. schedule was abruptly eliminated, it is thought that such customers would begin purchases under the Commercial-Industrial Power (C.I.P.) schedule. The C.I.P. schedule had the same demand energy form and level of rates as did the L.P. schedule. However, the minimum charges of the C.I.P. schedule was higher than that in the L.P. schedule and would cause customers affected to experience a higher per unit cost of electricity under the C.I.P. schedule if the load factor of purchases fell below a certain level. Those coal mines which purchased power under the L.P. schedule would be adversely affected by its deletion if they were relatively low load factor customers. We cannot eliminate the L.P. schedule on the basis of the record before us.

C.P. Rate Schedule

Appalachian proposes the deletion of the Capacity Power rate schedule available to industrial power users (other than coal mines). The C.P. schedule is a primary-secondary type rate, with two sets of declining block rates keyed to use and to the customers' contracts for electric capacity in amounts over 50 KVA and in multiples of 25 KVA. The C.P. rate was apparently designed for the low load factor industrial customer.

The elimination of the C.P. schedule on and after August 28, 1975, forced the C.P. customers to elect between the General Service (G.S.) and the Commercial-Industrial Power (C.I.P.) rate schedules.

The impact of Appalachian's filing is illustrated by the plight of the letter-Protestant, Guyan Machinery Co. ("Guyan") of Logan, West Virginia. Guyan protests that they were forced to purchase under the C.I.P. schedule after August 28, 1975, because Appalachian's G.S. schedule was "plain murder" and Guyan's low use made unavailable the other Appalachian schedules granted coal mines and other large volume users. Guyan complained that being forced to go to the C.I.P. schedule gave them a "double" increase, that is, (1) an increase resulting from going from the more-favorable C.P. to the C.I.P. schedule, plus (2) the rate increase proposed for the C.I.P. schedule.

The creation of several classes of service depends upon a combination of distinctive load characteristics (magnitude of demand, load factor, time of use, frequency and duration), as well as special physical circumstances of large industrial demands and purchases in relation to the utility's facilities and capacity. The nature of the customer's functions or its societal context as an industry, commercial business, school, church or other institution is also important in justifying *reasonable* rate differentials and separate rate forms.

As a general rule the Commission favors a reduction in the number of rate schedules in a tariff in order to simplify the administration, regulation and understanding of customer billings. However, we do not approve the deletion of rate schedules, which certain customers have come to rely upon, without something more tangible and persuading than the mere simplification of a tariff.

We must have more than a mere assertion that certain rate forms were "promotional" and are deleted because they were "designed years ago to serve coal mining customers and which cannot be justified on a cost of service basis in today's economic climate". The record does not support this assertion. We suggested in Case No. 7083 by our order issued January 31, 1975, rate changes should not be abrupt in departing from historical rates because customers in various classes of service have geared themselves to rates and rate forms in effect. An abrupt change would destroy this relationship without good cause and do violence to the maintenance of good faith between the utility and its customers.

We will require that the C.P. and L.P. rate schedules be reinstituted and that the respective C.P. and L.P. customers who purchased under these rate schedules when they were last effective will have the option of choosing to be billed thereunder at the higher rates allowed herein for the period after August 28, 1975, and to receive refunds accordingly.

Gradual Elimination of Certain Services

Appalachian proposes to gradually eliminate its Church Service (C.S.), School Service (S.S.) and Electric Heating-General (E.H.G.). It would phase out these rates over a 4-year period by imposing a cumulative 10% surcharge each twelve months for the period ending August 27, 1979. At some point before the end of the 4-year period Appalachian would anticipate that its customers, severally, would find it economically advantageous to shift to the G.S., C.I.P. or P.S.O. (Public School Optional) schedules.

Here, too, no cost apportionment by classes was presented on the evidentiary record. The schools, churches and general service (non-residential) heating customers have been paying higher declining block rates, plus a 10% surcharge in 1975-1976 and a 20% surcharge in 1976-1977. The Commission is informed that certain of these customers, including the churches, have had demand meters installed by Appalachian.

Protestant, Kanawha Valley Baptist Association, through its moderator, Mrs. Lucille E. Gillispie, presented evidence and argued persuasively that the elimination of the C.S. schedule was demonstrably unjust. The Staff of the Commission agrees and noted Mrs. Gillispie's testimony that the "concept of the demand meter is prejudicial against churches which have activities primarily on one day, and that day being when industry is at its lowest ebb".

We find that the churches and schools are distinctive institutions dissimilar in character from the residential, commercial and industrial institutions in several ways that have relevance to utility service and pricing with reference to load characteristics, economics, philosophy of pricing, and societal context.

We find that E.H.G. service, as well as C.S. and S.S. service cannot be eliminated, even gradually, without a consideration of the cost of such service in relation to what each is reasonably worth.

Appalachian will be required to reinstate the C.S., S.S. and E.H.G. rate schedules without the surcharge and at the lower block rates determined in this order and refund to the respective customers the entire surcharges collected, plus the difference in the filed block rates and the lower approved block rates. Our action here has support in principle under *Clarksburg Light and Heat Co.* v *P.S.C. of W. Va.*, 84 W.Va. 638, 100 SE 551 (1919); *Anchor Coal Co. et al* v *P.S.C. of* W. Va. [sic], 123 W. Va. 439, 15SE 2d 406 (1941).

Other Tariff Provisions

Appalachian also filed two new schedules, R.E. (Rural Line Extension Plan) and T.S. (Temporary Service). In Staff's brief we are urged to approve for West Virginia, the wording of Appalachian's Virginia tariff relating to extension of service as being more specific. Staff also urges that "residential customers" should be excluded from certain limitations in the tariff provisions related to "Service Connections" and "Use of Energy By Customer", which are sections in tariff's "Terms and Conditions of Service". Finally, Staff urges that residential customers who have their service discontinued, should be excused thereafter from paying any minimum bill. These suggested changes do not appear to be opposed by Appalachian or the other parties to the proceeding and are approved. They are in the public interest and some will be further modified so that Appalachian's tariff will be in conformance with our recently promulgated Rules and Regulations for the Government of Electric Utilities.

Although not raised in any of the briefs, we note that Appalachian has changed the form of its minimum monthly charge for its L.C.P. service. The record is void of any support for this change in rate design. Appalachian will be required to revert to the *form* of minimum charges contained in its tariff sheets in effect April 1, 1975 through August 27, 1975, without prejudice to changing its minimum charges in future rate proceedings upon a consideration of costs and other pertinent factors.

The specific tariff provisions discussed and required to be modified are set forth in Appendix G hereto.

FINDINGS

In addition to the decisional findings and conclusions above, the Commission finds as follows:

1. The rates and charges set forth in Appalachian Power Company's Tariff W.Va. P.S.C. No. 3 issued March 31, 1975,

and put into effect August 28, 1975, by terms of West Virginia Code, Chapter 24, Article 2, Section 4, are unjust and unreasonable for the reason that they would produce more revenues than are necessary to enable Appalachian Power Company to pay its reasonable and necessary operating expenses, taxes, and depreciation, and earn a fair return on its property used and useful in its public service business in the State.

2. Appalachian Power Company did not sustain its burden of proof to avoid undue rate discrimination under West Virginia Code, Chapter 24, Article 2, Section 2, so as to justify its proposed modifications in the rate forms contained in the R.S., L.C.P., C.S., E.H.G. and S.S. schedules and its proposed deletions of the C.P. and L.P. schedules as of and after August 28, 1975.

3. The changes proposed by Appalachian Power Company in the "Terms and Conditions of Service" portion of its filed tariff on Original Sheet Nos. 3-1, 3-2, 3-3, 3-4 and 3-5, are not supported by the evidence and are not in the public interest to the extent that they may substantially depart from Part 4.00 Customer Relations of the Rules and Regulations for the Government of Electric Utilities promulgated by this Commission as of March 1, 1977, and soon to be in effect in May 1977 and thereafter, unless modified.

4. The rates, charges and tariff provisions hereinafter approved, are just, reasonable and not unduly discriminatory.

Order

1. The tariff sheets filed with the Commission by the respondent, in its Tariff W.Va. P.S.C. No. 3, issued March 31, 1975, are hereby cancelled and stricken from the tariff files of the Commission, except for Original Sheet Nos. 2-1, 2-2, 2-3, 2-4, 2-5, 12-1, 12-2 and 13.

2. The rates, charges and tariff provisions set out in Appendix F, Columns IV and V and Appendix G attached to this order are approved, severally, to become effective on and after August 28, 1975 and May 1, 1976, as shown or required therein.

3. Appalachian is ordered to utilize the *form* of minimum monthly charges as is contained in its tariff sheets approved by our Order issued August 9, 1976 in Case No. 7083, in the schedules to be filed.

4. Appalachian is ordered to file revised tariff sheets to supersede those sheets requiring modifications for its W.Va. P.S.C. Tariff No. 3, within fifteen (15) days of the date of this order for approval by this Commission as to their conformity with the findings and conclusions stated herein.

5. Appalachian shall refund to each of its customers entitled thereto, within sixty (60) days of the date of this order the amount of excess collected under the rates placed into effect under bond and the amount which would have been collected under the rates that are herein approved, with interest thereon, at the rate of seven and three-quarters per cent (7¾%) per annum, until paid; that refunds of Five Dollars ($5.00) or less may be made by crediting the amount of the subscriber's account, and that as to amounts in excess of Five Dollars ($5.00) the refund shall be made by check.

The respondent shall report to the Commission the amount refunded, including the interest, the manner of refunding and the amount, if any, which it has been unable to refund.

6. Appalachian shall rebill each customer, who had been billed under the C.P., L.P., C.S., S.S., or E.H.G. schedules prior to August 28, 1975 for the two periods which began

August 28, 1975 and May 1, 1976, so as to give the customer the option of requesting and receiving refunds under the prior rate form or the schedule under which the customer actually purchased power during the two refund periods.

7. Appalachian is hereby ordered to file in any of its future rate adjustment filings for service to West Virginia's retail customers, as part of its Tariff Rule 42 data, at least two cost apportionment studies, which will set forth fully-distributed cost responsibilities to West Virginia, Virginia and the Federal Power Commission jurisdictions and as to Appalachian's various classes of service; one study shall be on either a coincidental or non-coincidental peak basis and the other study shall be on the Excess Demand method.

A COPY.

TESTE:

s/ S. Grover Smith, Jr.
S. GROVER SMITH, JR.,
Secretary

APPENDIX A (CASE NO. 8182)

APPALACHIAN POWER COMPANY

BALANCE SHEET—YEAR END RATE BASE AND CAPITALIZATION AT 12/31/74

	Balance Sheet at December 31, 1974 (In Thousands)			Appalachian Rate Base Calculation December 31, 1974 (In Thousands)		Appalachian Capitalization at December 31, 1974 (In Thousands)	
ASSETS AND OTHER DEBITS							
Utility Plant		1,475,026		1,475,026			
Construction Work in Progress		104,201		104,201			
Total Utility Plant		1,579,227		1,579,227			
Accumulated Provision for Depreciation		(355,740)		(355,740)			
Net Plant			1,223,487	1,223,487			
Other Property			75,170				
Current Assets			176,423	68,556	*Prepayments, Materials & Supplies		
Deferred Debits			47,232				
Total Assets and Other Debits			1,522,312				
LIABILITIES AND OTHER CREDITS							
First Mortgage Bonds	669,748					669,748	Long-Term Debt
Debt Premiums	1,936	671,684					
Sinking Fund Debentures	40,153					40,153	Sinking Fund Debentures
Debt Premiums	229						
Sinking Fund Requirement	(468)	39,914					
Installment Purchases		24,000				24,000	Installment Purchase Contracts
Total Long-Term Debt			735,598				
Preferred Stock			109,799			109,799	Preferred Stock
Common Stock			117,958			117,958	Common Equity
Other Paid-In Capital			159,168			159,168	Common Equity
Retained Earnings			110,899			110,899	Common Equity
Current Liabilities			244,373			126,090	Short-Term Debt
Deferred Credits			44,517	(7,803)	Deferred Federal Income Tax-Liberalized Dep.	19,048	Deferred Fed. Inc. Tax —Accelerated Amortization
Total Liabilities and Other Credits			1,522,312				
				33,779	*Working Cash Allowance	20,588	Common Equity—Subsidiary Earnings
				1,318,019	Total Rate Base	1,397,451	Total Capital

* Calculated

APPENDIX B (CASE NO. 8182)

APPALACHIAN POWER COMPANY

COST OF SERVICE COMPONENTS AND REVENUE DEFICIENCY PER COMMISSION ORDER
TEST YEAR 1974
WEST VIRGINIA OPERATIONS
FIRST TIER

A. COST OF SERVICE COMPONENTS

	Operating Revenues	Operating Expenses	Depreciation and Amortization	Taxes—Other Than Federal Income Tax	Average Rate Base
	$	$	$	$	$
Per Staff Exhibit No. 8	176,075,074	105,990,991	17,334,859	16,023,424	488,448,552
Adjustments:					
Coal Expense @ 1.00 per MBTU		120,512			
April, 1975 Wage Increase		779,515			
Payroll Tax Adjustment				46,592	
Working Cash Adjustment Resulting From Operating Expense Adjustments					102,443
As Adjusted	176,075,074	106,891,018	17,334,859	16,070,016	488,550,995

B. COST OF SERVICE AND REVENUE DEFICIENCY

Allowance for Return @ 9.35%	$ 45,679,518
Operation and Maintenance Expenses	106,891,018
Depreciation and Amortization	17,334,859
Federal Income Tax	4,573,249*
Other Taxes—Before Additional Business and Occupation Tax	16,070,016
Additional Business and Occupation Tax	916,663*
Total Cost of Service	$191,465,323
Revenue Deficiency	$ 15,380,249

NOTE: * Calculated After Other Adjustments.

APPENDIX C (CASE NO. 8182)

APPALACHIAN POWER COMPANY

COST OF SERVICE COMPONENTS AND REVENUE DEFICIENCY PER COMMISSION ORDER
TEST YEAR 1974
WEST VIRGINIA OPERATIONS
SECOND TIER

A. COST OF SERVICE COMPONENTS

	Operating Revenues	Operating Expenses	Depreciation and Amortization	Taxes Other Than Federal Income Tax	Average Rate Base
	$	$	$	$	$
As Adjusted for Period from August 20, 1975 through April 30, 1976 ..	176,075,074	106,891,018	17,334,859	16,070,016	488,550,995
Adjustments:					
Coal Expense @ 1.04¢ per BTU		3,042,433			
April, 1976 Wage Adjustment		1,147,678			
Insurance and Postage Adjustment		236,755			
Increase in F.I.C.A. Base				77,396	
Payroll Taxes on April Wage Adjustment..				68,597	
Working Cash Adjustment					425,912
As Adjusted	176,075,074	111,317,884	17,334,859	16,216,009	488,976,907

B. COST OF SERVICE AND REVENUE DEFICIENCY

Allowance for Return @ 9.25%	$ 45,719,341
Operation and Maintenance Expenses	111,317,884
Depreciation and Amortization	17,334,859
Federal Income Tax	4,596,410*
Other Taxes—Before Additional Business & Occupation Tax	16,216,009
Additional Business and Occupation Tax	1,210,470*
Total Cost of Service	$196,394,973
Revenue Deficiency	$ 20,309,899

* Calculated after other adjustments.

APPENDIX D

APPALACHIAN POWER COMPANY

CASE No. 8182

COMPARISON OF JURISDICTIONAL DELIVERIES AND UNIT REVENUES

1971-1976

	West Virginia			Virginia			Federal Power Commission Jurisdiction										
							Account 447—Sales For Resale			Interchange-Out To Affiliates			Interchange-Out Non-Affiliates				
	Volume	Revenue	Revenue/ Kwh	Volume	Revenue	Revenue/ Kwh	Volume	Revenue	Revenue/ Kwh	Volume	Receipts	Receipts/ Kwh	Volume	Receipts	Total Volume	Receipts/ Kwh*	
	Mwh	(000) $	¢	Mwh	(000) $	¢	Mwh	(000) $	¢	Mwh	(000) $	¢	Mwh	(000) $			
1971	7,407,817	99,554	1.34	6,216,874	89,532	1.44	3,786,979	34,785	.92	2,140,368	15,053	.70	573,872	Not Available	6,501,219	.84	
1972	7,661,245	109,044	1.42	6,512,655	98,818	1.52	4,793,612	44,927	.94	6,974,529	39,828	.57	505,914	Not Available	12,274,055	.72	
Increase—1971	3.4	9.5	6.0	4.8	10.4	5.6	26.6	29.2	2.2	225.9	164.6	(18.6)	(12.0)		88.8	(14.3)	
1973	8,043,103	118,586	1.47	7,091,705	109,523	1.54	5,681,406	52,169	.92	8,835,857	52,473	.59	587,121	Not Available	15,104,384	.72	
Increase—1971	8.6	19.1	9.7	14.1	22.3	6.9	50.0	50.0	0.0	312.8	248.6	(15.7)	2.3		132.3	(14.3)	
1974	8,225,366	169,106	2.06	7,244,332	156,902	2.17	5,704,296	86,203	1.51	7,902,412	97,272	1.23	710,300	Not Available	14,317,008	1.35	
Increase—1971	11.0	69.9	53.7	16.5	75.2	50.7	50.6	147.8	64.1	269.2	546.2	75.7	23.8		120.2	60.7	
1975	8,175,885	203,248	2.48	7,356,712	184,022	2.50	6,824,645	113,642	1.67	6,654,970	78,908	1.19	606,466	Not Available	14,086,081	1.43	
Increase—1971	10.4	104.2	85.1	18.3	105.5	73.6	80.2	226.7	81.5	210.9	424.2	70.0	5.7		116.7	70.2	
1976	8,745,946	230,789	2.64	7,875,839	212,007	2.69	9,159,250	156,897	1.71	5,961,996	77,806	1.30	623,347	Not Available	15,744,593	1.55	
Increase—1971	18.1	131.8	97.0	26.7	136.8	86.8	141.9	351.0	85.9	178.6	416.9	85.7	8.6		142.2	84.5	

NOTE: *Average of Credits to Account 447 and Interchange-Out to Affiliates

Recapitulation of FPC Jurisdictional Energy Sales

	1971	1976	Incremental Growth
	Mwh	Mwh	Mwh
Sales for Resale	3,786,979	9,159,250	5,372,271
Interchange-Out			
—Affiliates	2,140,368	5,961,996	3,821,628
—Non-Affiliates	573,872	623,347	49,475
	6,501,219	15,744,593	9,243,374

Recapitulation of Total Energy Sales

	1971	1976	Incremental Growth	Percent
	Mwh	Mwh	Mwh	%
West Virginia	7,407,817	8,745,946	1,338,129	18.1
Virginia	6,216,874	7,875,839	1,658,965	26.7
Federal Power Commission	6,501,219	15,744,593	9,243,374	75.9
	20,125,910	32,366,378	12,240,468	100.0

APPENDIX E

APPALACHIAN POWER COMPANY

ENERGY—KWH—WEST VIRGINIA

Year	Residential	Incremental % From 1971	Commercial	Incremental % From 1971	Industrial	Incremental % From 1971	Other*	Incremental % From 1971	Total	Incremental % From 1971
1971 ...	1,758,171,438	—	1,180,762,191	—	4,444,695,756	—	95,238,512	—	7,478,867,897	—
1972 ...	1,897,943,511	7.9	1,277,480,451	8.2	4,460,818,707	0.3	100,160,011	5.1	7,736,402,680	3.4
1973 ...	2,119,631,626	20.6	1,388,133,247	17.6	4,509,108,839	1.5	99,153,320	4.1	8,116,027,032	8.5
1974 ...	2,759,265,580	28.5	1,376,687,421	16.6	4,562,796,849	2.7	101,332,651	6.4	8,300,082,501	11.0
1975 ...	2,412,918,831	37.2	1,462,180,687	23.9	4,271,990,226	(3.9)	109,855,026	15.3	8,256,944,770	10.4
1976 ...	2,642,568,133	50.3	1,560,540,509	32.2	4,512,265,998	1.5	117,998,446	23.8	8,833,373,086	18.1

NOTE: * Includes Public Street Lighting, Other Sales to Public Authorities and Sales for Resale.

APPENDIX E—(Continued)

APPALACHIAN POWER COMPANY

REVENUE—$—WEST VIRGINIA

Year	Residential	Incremental % From 1971	Commercial	Incremental % From 1971	Industrial	Incremental % From 1971	Other*	Incremental % From 1971	Total	Incremental % From 1971
1971	36,720,127	—	22,579,790	—	42,000,677	—	1,672,022	—	102,972,616	—
1972	42,746,386	16.4	26,230,008	16.2	47,643,707	13.4	1,793,579	7.2	118,413,680	15.1
1973	47,391,095	29.1	28,709,876	27.2	50,479,767	20.2	1,951,371	16.7	128,532,109	24.9
1974	63,681,382	73.4	36,892,668	63.4	77,588,301	84.7	2,455,118	46.8	180,617,469	75.5
1975	77,669,551	111.5	45,520,195	101.7	92,740,903	120.8	2,804,675	67.7	218,735,324**	112.5
1976	85,071,837	131.6	49,558,673	119.5	94,893,789	125.9	2,821,471	68.7	232,345,770	125.7

NOTE: * Includes Public Street Lighting, Other Sales to Public Authorities and Sales for Resale.

** Includes 7,041,808 Estimated Overrecovery of Fuel Component.

APPALACHIAN POWER COMPANY

Comparison of Rates

	I	II	III	IV	V
				Final Commission Approved Rates—Case No. 8182	
	Rates filed pursuant to order dated 8/9/76 in Case No. 7083. Reopened Effective 4/1/75-8/27/75	Lawful Base Rates as of 8/27/75*	Net Rates filed in Case No. 8182**	Effective 8/28/75 through 4/30/76	Effective on and after 5/1/76
	¢/Kwh	¢/Kwh	¢/Kwh	¢/Kwh	¢/Kwh
Tariff C.L.P. (Combined Light & Power)	Since no customers were being served under this rate schedule it was not submitted by the company.		Discontinued		Discontinued
Primary (50 x Capacity)					
Secondary (Excess over Primary)					
First 5,000 Kwhrs					
Next 5,000 Kwhrs					
Over 10,000					
Minimum Charge					
Tariff R.S. (Residential Service)					
First 30 Kwhrs per month	6.169	5.918	6.92426	5.918	5.918
Next 40	5.156	4.905	6.01326	5.338	5.476
Next 130	3.535	3.284	4.07626	3.574	3.666
Next 300	2.623	2.372	2.93726	2.581	2.648
Next 1,000	2.319	2.068	2.48126	2.251	2.309
Over 1,500	2.116	1.865	2.25326	2.030	2.082
Minimum	$ 1.50	$ 1.50	$ 2.50	$ 2.50	$ 2.50
Water Heater Service					
Last 400 Kwhrs per month	2.116	1.865	2.25326	2.030	2.082
Tariff G.S. (General Service)					
50 x Monthly Demand					
First 30 Kwhrs	6.169	5.918	7.31226	6.456	6.630
Over 30	4.903	4.652	5.73926	5.078	5.217
Next 150 x Monthly Demand					
First 3,000 Kwhrs	3.535	3.284	4.03126	3.590	3.689
Over 3,000	2.623	2.372	2.90326	2.597	2.671
Over 200 x Monthly Demand	2.116	1.865	2.26526	2.046	2.105
Minimum Charge	$ 1.50	$ 1.50	$ 2.50	$ 2.50	$ 2.50

Notes:

* Not filed because of coincidental effectiveness of proposed No. 8182 rates.

** Filed rates adjusted for credit of .25074¢/Kwh.

APPALACHIAN POWER COMPANY

Comparison of Rates

	I	II	III	IV	V
				Final Commission Approved Rates—Case No. 8182	
	Rates filed pursuant to order dated 8/9/76 in Case No. 7083. Reopened Effective 4/1/75-8/27/75	Lawful Base Rates as of 8/27/75*	Net Rates filed in Case No. 8182**	Effective 8/28/75 through 4/30/76	Effective on and after 5/1/76
	¢/KWH	¢/KWH	¢/KWH	¢/KWH	¢/KWH
Tariff C.I.P. (Commercial-Industrial) formerly C.P.O. (Capacity Power-Optional)					
First 30 x Monthly Demand	5.566	5.315	6.56026	5.800	5.957
Next 170 x Monthly Demand:					
First 3,000 Kwhrs	3.266	3.015	3.70026	3.297	3.389
Next 3,000	3.064	2.813	3.44926	3.077	3.164
Next 4,000	2.861	2.610	3.19926	2.856	2.937
Next 10,000	2.658	2.407	2.93726	2.636	2.711
Next 80,000	2.456	2.205	2.68626	2.416	2.485
Over 100,000	2.253	2.002	2.43626	2.195	2.258
Next 160 x Monthly Demand	1.858	1.607	1.94626	1.765	1.817
Over 360 x Monthly Demand	1.655	1.404	1.69526	1.544	1.591
Minimum Charge	$ 2.00/KVA	$ 2.00/KVA	$ 2.00/KVA	$ 2.00/KVA	$ 2.00/KVA
Tariff P.S.O. (Public School-Optional)					
All Energy	3.636	3.385	4.14926	3.700	3.803
Minimum Charge	$ 2.50	$ 2.50	$ 2.50	$ 2.50	$ 2.50
Tariff E.H.G. (Electric Heating General)					
First 200 Kwhrs	4.143	3.892	4.78826	4.281	4.368
Next 6,800	2.623	2.372	2.90326	2.597	2.671
Over 7,000	2.319	2.068	2.51526	2.267	2.332
Each Kw Demand in Excess of 30	$ 1.27	$ 1.27	$ 1.57	$ 1.38	$ 1.42
Minimum Charge	$ 8.29	$ 7.78	$10.08	$ 8.56	$ 8.74
Tariff S.S. (School Service)					
First 500 Kwhrs per Classroom	3.636	3.385	4.19026	3.700	3.803
Balance	1.812	1.561	1.91126	1.715	1.766
Minimum Charge	$ 2.50	$ 2.50	$ 2.50	$ 2.50	$ 2.50

Notes:

* Not filed because of coincidental effectiveness of proposed No. 8182 rates.

** Filed rates adjusted for credit of .25074¢/Kwh.

APPENDIX F—(Continued)

APPALACHIAN POWER COMPANY

Comparison of Rates

	I	II	III	IV	V
	Rates filed pursuant to order dated 8/9/76 in Case No. 7083. Reopened Effective 4/1/75-8/27/75	Lawful Base rates as of 8/27/75*	Net Rates filed in Case No. 8182**	Final Commission Approved Rates—Case No. 8182 Effective 8/28/75 through 4/30/76	Final Commission Approved Rates—Case No. 8182 Effective on and after 5/1/76
	¢/KWH	¢/KWH	¢/KWH	¢/KWH	¢/KWH
Tariff C.S. (Church Service)					
First 40 KWHrs per month	6.169	5.918	7.31226	6.456	6.630
Next 85	5.156	4.905	6.04726	5.354	5.499
Next 375	3.839	3.588	4.40626	3.921	4.029
Next 500	2.927	2.676	3.27926	2.928	3.011
Over 1,000	2.623	2.372	2.90326	2.597	2.671
Minimum Charge	$ 1.50	$ 1.50	$ 2.50	$ 2.50	$ 2.50
Tariff C.P. (Capacity Power—Wholesale)			Discontinued		
100 x Contract Capacity:					
100 x First 50 Kva	4.290	4.039	"	4.411	4.533
100 x Next 50 Kva	3.884	3.633	"	3.969	4.079
100 x Next 50 Kva	2.871	2.620	"	2.867	2.948
100 x Next 150 Kva	2.669	2.418	"	2.647	2.723
100 x Over 300 Kva	2.466	2.215	"	2.426	2.496
Excess of 100 x Capacity:			"		
First 50,000 KWHrs	2.456	2.205	"	2.415	2.485
Next 50,000	2.354	2.103	"	2.304	2.371
Next 200,000	2.253	2.002	"	2.194	2.258
Over 300,000	2.203	1.952	"	2.140	2.203
Minimum Charge	$24.00/KVA	$24.00/KVA	"	$25.95/KVA	$26.80/KVA

Notes:

* Not filed because of coincidental effectiveness of proposed No. 8182 rates.

** Filed rates adjusted for credit of .25074¢/KWH.

APPENDIX F—(Continued)

APPALACHIAN POWER COMPANY

Comparison of Rates

	I	II	III	IV	V
				Final Commission Approved Rates—Case No. 8182	
	Rates filed pursuant to order dated 8/9/76 in Case No. 7083. Reopened Effective 4/1/75-8/27/75	Lawful Base Rates as of 8/27/75*	Net Rates filed in Case No. 8182**	Effective 8/28/75 through 4/30/76	Effective on and after 5/1/76
	¢/Kwh	¢/Kwh	¢/Kwh	¢/Kwh	¢/Kwh
Tariff T.P. (Transmission Power)					
For 34.5-69 KV Delivery Voltage					
First 25,000 KVA Demand	$ 6.076	$ 5.324	$ 6.46478	$ 5.793	$ 5.943
Over 25,000 KVA Demand	$ 5.832	$ 5.080	$ 6.15678	$ 5.528	$ 5.671
For 138 KV Delivery Voltage					
First 25,000 KVA Demand	$ 5.934	$ 5.182	$ 6.28178	$ 5.639	$ 5.785
Over 25,000 KVA Demand	$ 5.782	$ 5.030	$ 6.09978	$ 5.473	$ 5.615
Secondary—All Voltage					
Energy in Excess of 300 Kwhrs per KVA Demand	$ 0.01448	$ 0.01197	$ 0.0143326	$ 0.01318	$ 0.01360

NOTES:

* Not filed because of coincidental effectiveness of proposed No. 8182 rates.

** Filed rates adjusted for credit of .25074¢/Kwh.

APPALACHIAN POWER COMPANY

Comparison of Rates

	I	II	III	IV	V
				Final Commission Approved Rates—Case No. 8182	
	Rates filed pursuant to order dated 8/9/76 in Case No. 7083. Reopened Effective 4/1/75-8/27/75	Lawful Base Rates as of 8/27/75*	Net Rates Filed in Case No. 8182**	Effective 8/28/75 through 4/30/76	Effective on and after 5/1/76
	¢/KWH	¢/KWH	¢/KWH	¢/KWH	¢/KWH
Tariff L.P. (Large Power)					
First 30 x Monthly Demand	5.566	5.315	Discontinued	5.7994	5.957
Next 170 x Monthly Demand:					
First 3,000 Kwhrs	3.266	3.015	"	3.297	3.389
Next 3,000	3.064	2.813	"	3.077	3.164
Next 4,000	2.861	2.610	"	2.856	2.937
Next 10,000	2.658	2.407	"	2.635	2.710
Next 80,000	2.456	2.205	"	2.415	2.485
Over 100,000	2.253	2.002	"	2.194	2.258
Next 160 x Monthly Demand	1.858	1.607	"	1.765	1.817
Over 360 x Monthly Demand	1.655	1.404	"	1.544	1.591
Minimum Charge	$ 1.30/Kva	$ 1.30/Kva	"	$ 1.41	$ 1.45
Tariff L.C.P (Large Capacity Power)					
First 1,000 Kw Monthly Demand	$ 7.463	$ 6.673	$ 8.141	$ 7.261	$ 7.450
Next 3,000	$ 6.967	$ 6.177	$ 7.514	$ 6.722	$ 6.896
Over 4,000	$ 6.450	$ 5.660	$ 6.876	$ 6.159	$ 6.319
Energy in Excess of 315 Kwhrs Per Kw Demand	$ 0.01579	$ 0.01328	$ 0.0160426	$ 0.01461	$ 0.01506
Reactive Demand Charge	$ 0.25	$ 0.25	$ 0.32	$ .27	$ 0.28
Tariff I.R.P. (Interruptible Power)					
Demand Charge:					
Kw Demand	$ 0.676	$ 0.676	$ 0.841	$ 0.736	$ 0.755
Kvar Demand	$ 0.25	$ 0.25	$ 0.32	$ 0.27	$ 0.28
Energy Charge	$ 0.01499	$ 0.01248	$ 0.0149926	$ 0.01374	$ 0.01417

Notes:

* Not filed because of coincidental effectiveness of proposed No. 8182 rates.

** Filed rates adjusted for credit of .25074¢/KWH.

APPALACHIAN POWER COMPANY

Comparison of Rates

	I	II	III	IV	V
				Final Commission Approved Rates—Case No. 8182	
	Rates filed pursuant to order dated 8/9/76 in Case No. 7083. Reopened Effective 4/1/75-8/27/75	Lawful Base rates as of 8/27/75*	Net Rates filed in Case No. 8182**	Effective 8/28/75 through 4/30/76	Effective on and after 5/1/76
	¢/Kwh	¢/Kwh	¢/Kwh	¢/Kwh	¢/Kwh
Tariff H.L.P. (High Load Factor Power)					
For 34.5-69 KV Delivery Voltage					
First 67,000 KW Demand	$10.287	$ 8.783	$10.61456	$ 9.557	$ 9.805
Next 33,000 KW	$10.044	$ 8.540	$10.30656	$ 9.293	$ 9.534
Over 100,000 KW	$ 9.922	$ 8.418	$10.15856	$ 9.160	$ 9.397
For 138 KV Delivery Voltage					
First 67,000 KW Demand	$10.206	$ 8.701	$10.51156	$ 9.468	$ 9.714
Next 33,000 KW	$ 9.993	$ 8.488	$10.23856	$ 9.238	$ 9.477
Over 100,000 KW	$ 9.873	$ 8.368	$10.09056	$ 9.105	$ 9.341
Secondary—All Voltage					
Energy in Excess of 600 KWHrs per KW Demand	$ 0.01411	$ 0.01160	$ 0.0138720	$ 0.01279	$ 0.01318
Demand Charge	$ 0.25	$ 0.25	$ 0.32	$ 0.27	$ 0.28
Tariff O.L. (Outdoor Lighting)					
Each 7,000 Lumen Mercury	$ 4.22	$ 4.74	$ 5.92	$ 5.16	$ 5.29
Each 11,000 Lumen Mercury	$ 5.53	$ 6.25	$ 7.83	$ 6.80	$ 6.98
Each 20,000 Lumen Mercury	$ 6.59	$ 7.74	$ 9.81	$ 8.42	$ 8.64
Each 2,500 Lumen Incandescent	$ 3.16	$ 3.63	$ 4.58	$ 3.95	$ 4.05
Each 4,000 Lumen Incandescent	$ 3.69	$ 4.42	$ 5.65	$ 4.81	$ 4.93
Each 7,000 Lumen Mercury on 12′ Post	$ 5.00	$ 5.52	$ 6.87	$ 6.00	$ 6.16
Rider A (Credit Surcharge)					
Credit applied to RS, GS, CS, CP, CIP, PSO, EHG, TP, SS, LP, LCP, IRP & HLP for each Kwh used	$ .0000673	Not Applicable	Not Applicable	Not Applicable	Not Applicable

NOTE:

* Not filed because of coincidental effectiveness of proposed No. 8182 rates.

** Filed rates adjusted for credit of .25074¢/Kwh.

APPENDIX F—(Continued)

APPALACHIAN POWER COMPANY

Comparison of Rates

	I	II	III	IV	V
	Rates filed pursuant to order dated 8/9/76 in Case No. 7083. Reopened Effective 4/1/75-8/27/75	Lawful Base rates as of 8/27/75*	Net Rates filed in Case No. 8182**	Final Commission Approved Rates—Case No. 8182 Effective 8/28/75 through 4/30/76	Final Commission Approved Rates—Case No. 8182 Effective on and after 5/1/76
	¢/KWH	¢/KWH	¢/KWH	¢/KWH	¢/KWH
Tariff R.E. (Rural Line Extension)					
Tariffs Applied	Applicable Tariff	Applicable Tariff	Applicable Tariff	Applicable Tariff	
Minimums:					
Per Customer Per Month	$ 2.50	$ 2.50	$ 4.00	$ 4.00	$ 4.00
Per Mile Per Month	$ 10.00	$ 10.00	$ 18.50	$ 18.50	$ 18.50
Minimum Excluded if Gross Annual Revenue Per Mile Exceeds	$500.00	$500.00	$775.00	$775.00	$775.00
Tariff T.S. (Temporary Service)					
Tariffs Applied	Applicable Tariff	Applicable Tariff	Applicable Tariff	Applicable Tariff	
Special Terms	Available in Cases Where Provisions of Applicable Tariff Would Normally Preclude Service of a Temporary Nature.				

APPENDIX G

APPALACHIAN POWER COMPANY
(CASE NO. 8182)

Certain portions of the "Terms and Conditions of Service" in Appalachian's tariff filing designated W.Va. P.S.C. Tariff No. 3 in Original Sheet Nos. 3-1, 3-2, 3-3, 3-4 and 3-5 are to be modified as follows:

Original Sheet No. 3-1

"APPLICATION"—This paragraph shall be broadened to comply with Section 4.01 (2) and (3) of the "Rules and Regulations for the Government of Electric Utilities" (referred to hereinafter as the "Electric Rules") promulgated by the Commission as of March 1, 1977.

"DEPOSITS"—This paragraph shall be modified to conform with Section 4.02 of the Electric Rules of the Commission.

Original Sheet Nos. 3-1 and 3-2

"PAYMENTS"—This section shall be broadened to comply with Section 4.08 (1) (a) (4) of the Commissioner's Electric Rules requiring the utility to accept payment at the customer's premises in lieu of discontinuing service.

Original Sheet No. 3-2

"SERVICE CONNECTIONS"—This section shall be modified to exclude residential customers from the requirement that the customer's wiring shall be brought outside the building wall nearest the Company's service wires. Moreover, our ruling on this section, is subject to Order in pending Case No. 8455, involving the Company, which will be issued soon.

Original Sheet No. 3-3

"COMPANY'S LIABILITY"—This section is subject to our Order in pending Case No. 8455, which will be issued soon.

Sheet 2 of 2
(Appendix G)

Original Sheet Nos. 3-3 and 3-4

"Extension of Service"—This section shall be modified to contain the substance of Appalachian's tariff, Original Sheet Nos. 3-6 and 3-7 filed in Virginia as part of the Company's Va. S.C.C. Tariff No. 7, issued June 2, 1975.

Original Sheet No. 3-4

"Use of Energy by Customer"—This section shall be modified so as to (1) exclude residential customers from the requirement that customers shall not add to the equipment or load of the residence except by consent of the Company, (2) the Company shall be the "initial" judge, but *not* the "sole" judge as to the suitability of apparatus and appliances and (3) The Public Service Commission of West Virginia shall be the proper forum for any disputes under this section which cannot be satisfactorily settled between the Company and its customer.

Original Sheet No. 3-5

"Power Factor of Lighting Equipment"—This section shall be modified to comply with Section 5.07 of the Commission's Electric Rules.

"Domestic Service"—This section shall be modified to provide that larger motors may be served when in the Company's "initial", not "sole" judgment, the existing service facilities of the Company are adequate.

Original Sheet No. 3-5

"Denial or Discontinuance of Service"—This section shall be modified (1) to excuse residential customers whose service is discontinued for reasons stated in the section from paying a minimum bill after such discontinuance, and (2) the section shall be modified to conform to Section 4.08 of the Commission's Electric Rules.

Sheet 2 of 2
(Appendix G)
[Continued]

"Reconnection Charge"—This section shall be amended to reduce the reconnection charge for residential and general service customers to $5.50 as was contained in the tariff provisions in effect prior to the Company's W. Va. P.S.C. Tariff No. 3, because of failure of proof.

"General"—This section shall be amended to refer to the Commission's Electric Rules, revised as of March 1, 1977, and to be effective May 16, 1977.

PUBLIC SERVICE COMMISSION
OF WEST VIRGINIA

CHARLESTON

At a session of the PUBLIC SERVICE COMMISSION OF WEST VIRGINIA, at the Capitol in the City of Charleston on the 9th day of May, 1977.

CASE No. 8182

APPALACHIAN POWER COMPANY, a corporation.

In the matter of increased rates and charges.

CORRECTIVE ORDER

WHEREAS, by order entered herein on May 6, 1977, certain typographical errors have been noted and should be corrected, as follows:

Page 3—Third line from bottom, change "makes" to "make";
Page 4—Tenth line from bottom, change "Column I" to "Column II";
Page 33—Last line, change "75.9%" to 75.5%" [sic];
Page 34—First line, change "12,340,468,000" to "12,240,468,000 [sic];
Second line, change "18.1%" to "or 10.9% of total growth";
Third line, change "26.7% [sic] to "or 13.6% of total growth";
Third line from bottom, change "interchang-" to "interchange-";
Page 42—Eighth line, change "above" to "below";
Appendix C—under part B — change "9.25%" to "9.35%";
Appendix D—Under "Recapitulation of Total Energy Sales", Percent Column, change "18.1%" to

"10.9%" for W. Va.; "26.7%" to "13.6%" for Virginia and "75.9%" to "75.5%" for FPC; and
Appendix E, Sheet 1 of 2—change percentage growth in 1974 residential sales "28.5%" to "56.9%".

and that in all other respects, the said order of May 6, 1977, shall remain in full force and effect.

A COPY.

TESTE:

s/ S. Grover Smith, Jr.
S. GROVER SMITH, JR.
Secretary

PUBLIC SERVICE COMMISSION
OF WEST VIRGINIA

CHARLESTON

At a session of the PUBLIC SERVICE COMMISSION OF WEST VIRGINIA, at the Capitol in the City of Charleston on the 29th day of July, 1977.

CASE No. 8182

APPALACHIAN POWER COMPANY, a corporation.
In the matter of increased rates and charges.

ORDER DENYING IN PART AND GRANTING IN PART PETITION FOR REHEARING, REOPENING OF THE RECORD, AND REARGUMENT AND CLARIFYING ORDER ISSUED MAY 6, 1977.

POST-DECISIONAL PROCEDURE

On May 6, 1977, this Commission issued its final order covering a multitude of subsidiary issues in ratemaking, which allowed some rate relief but not all of the rate relief requested and, among other things, ordered Appalachian Power Company to refund excess collections of revenues with interest thereon at the annual rate of 7¾%.

On May 16, 1977, Appalachian filed its Petition for Rehearing, Reopening of the Record, and Reargument, with affidavits of Gerald P. Maloney, Morris E. McCrary, Peter J. DeMaria and Michael Brown McNulty, officers or employees of Appalachian or its affiliates. On May 23, 1977, Appalachian filed supplementary affidavits of Gerald Blackmore and Morris E. McCrary.

Appalachian's Petition for Rehearing, etc., requested modification of the Commission's order of May 6, 1977, to the effect that

(1) the rates determined upon a 9.35% rate of return were too low;

(2) the Commission had erred in its disposition of subsidiary issues pertaining to (a) consolidated tax savings, (b) capacity equalization adjustment, (c) jurisdictional cost allocation;

(3) the Commission should permit Appalachian to have a Third-Tier Rate Level increase effective May 1, 1977, on the basis of (a) purported increases in its cost of coal, (b) purported wage increases which became effective April 1, 1977, and (c) its continuing investment in pollution control facilities after August 1975; and

(4) the Commission should modify ordering paragraphs 4 and 5 of its order, so as (a) to give Appalachian 15 days after final determination on the relief requested by its Petition for Rehearing, etc., and (b) to delay the completion of refunds to a date 60 days from the date revised tariff sheets are finally approved by the Commission.

In addition, representatives of Appalachian informally raised the question with the Staff of the Commission as to how incidental details of the filed tariff sheets, not commented upon specifically in the Commission order, should be treated when the utility files its tariff sheets in compliance with our order. These incidental matters will be taken up on our own motion as a clarification of our order issued May 6, 1977.

COMMENT

We turn now to a discussion of the issues raised.

Consolidated Tax Saving

Appalachian's contentions against the Commission's order on the issue of the proper adjustment to Federal income tax to reflect a test year sharing of tax savings from filing a consolidated tax return by its parent, American Electric Power, Inc., are based upon a misunderstanding or misrepresentation of our order.

Appalachian erroneously characterizes the staff method approved by our order,—that the "approach assumes that the Parent's tax loss and thus the savings enjoyed by Appalachian will increase in proportion to increases in Appalachian's taxable income". This is Appalachian's view, not that of the Commission and its staff.

The method approved by the Commission is to use the *actual tax savings* associated with filing consolidated income tax returns over a three-year period prior to the test period in order to calculate a reasonable allowance for consolidated tax savings in ratemaking. Because of the many variables involved and the difficulty in projecting actual income tax savings to be experienced in future tax periods, the Commission exercises its discretion and judgment to make a fair adjustment for this cost item.

The Commission did *not* use "$4,100,837 of consolidated tax savings which was determined by applying a percentage factor (23%) to Appalachian's pro forma taxable income to derive Appalachian's allocated portion of the tax loss generated by Appalachian's Parent". Contrary to Appalachian's erroneous statement, the Commission reflected a tax savings for Appalachian of $1,197,747 for the first-tier rates and $1,204,818 for the second-tier rates, *not* $4,100,837. The recital of "$4,100,837 tax savings allocated to West Virginia" on page 28 of our order issued May 6, 1977, refers to a dollar figure based on the higher rates the Company asked for, and *not* on the lower rates the Commission granted.

Appalachian's rejected approach baldly assumes a non-variable Parent tax loss, without any evidentiary support.

We reject Appalachian's contentions on this issue and rely on the principle that where a projection of future Federal income tax savings is not known and measurable, the averaging method of projecting a tax savings is a conservative and fair way of determining the same.

Capacity Equalization Adjustment

Appalachian contends against the Commission's adjustment to test year purchased power expense in crediting adjusted (higher) test year revenues due to a June 1975 rate increase under the "Capacity Equalization Agreement" regulated by the Federal Power Commission. Its argument is grounded on its belief that by becoming a net purchaser of AEP System power after the test year, it should not have its test year purchased power expenses decreased by adjusted revenues based on a known and measurable FPC rate increase in June 1975 in the AEP System's Capacity Equalization Agreement.

Adjustments to test year revenues and expenses in ratemaking are largely discretionary to the regulator. In order to avoid arbitrary decisions, regulators usually confine their adjustments to "known and measurable" changes in revenues and costs. We followed that principle in our treatment of this issue. Appalachian, on the other hand, wants us to refrain from exercising our discretion, because of post-test year changes in AEP System power supply and usage which are ephemeral, and, even if "known", are *not* "measurable" within the context of the test year used in this proceeding.

Appalachian erroneously argues that the Commission is bound by one method of cost apportionment; namely, the "non-jurisdictional revenues credit to cost of service" method. To the contrary, not only are there many valid methods of jurisdictional cost apportionment, but also Appalachian's argument violates the recent teachings of the Supreme Court of the United States, to the effect that while one regulatory jurisdiction may lack authority to fix rates in another jurisdiction, it may determine the costs and take into account the rates in the other jurisdiction, when it fixes the rates in its own jurisdiction. See *FPC vs Conway Corporation,* US , 96 S Ct 1999 (1976). Indeed, the

very purpose of jurisdictional cost apportionment, where there is multiple regulation of a company, is for each jurisdiction to determine for itself the *fair* burdens that the customers it protects shall bear. In exercising this responsibility each jurisdiction has a broad discretion to use or not to use any number of cost apportionment methods, and each is *not* necessarily bound by the methods used by other jurisdictions, either Federal or State. If the Public Service Commission of West Virginia is not free to accept or reject the "revenue credit" method of cost apportionment, it would have lost an important element of its rate regulatory powers by the *indirect* encroachment of another regulatory body, and this would be counter to the intent of the various statutes which separate Federal and State rate regulation responsibilities.

The essence of Appalachian's argument is that it insists that this Commission cannot make any adjustments to test year figures, unless it makes all of the adjustments which are favorable to Appalachian, even though the basis for the additional adjustments are not *measurable* within the context of the 1974 test year.

For example, Appalachian makes a loose statement in its Petition that

> "The fact that Appalachian became a *capacity* deficient company within the AEP Power Pool in 1975 is a known change which even without Modification No. 3 substantially *increased* the Company's production expense over the test year level."

To the contrary, our regulation of Appalachian in the concurrent Cabin Creek Plant Case No. 8961 informs us that Appalachian was not a *capacity* deficient company within the AEP Power Pool in 1975, but instead started to become a *net purchaser of kilowatt-hours of energy* from the AEP Pool.

Appalachian continues its slant by stating that

> "Because of the difficulty of quantifying all the associated changes for ratemaking purposes, Appalachian has never sought an adjustment for this known change for test year experience."

Thus, this admission contains the general truth that an adjustment of gross sales and gross purchase volumes of energy *for the future,* resulting in a shift for Appalachian to become a *net seller* rather than a *net purchaser* of system power, are not only unpredictable, but more important, would reflect a total change in Appalachian and in system power supply and usage and concomitant revenues and costs. The Commission made a reasonable adjustment based on a "known and measurable" change in the FPC rate contained in the Capacity Equalization Agreement. Although *future* allocations in ratemaking may increase production expenses by the "revenue credit" method, also in that *future* rate case Appalachian may have purchased more power under its Capacity Equalization Agreement which it would have resold to its customers at a profit.

We reject Appalachian's assertions on this issue and reconfirm our discretionary adjustment to the production cost component in our order of May 6, 1977.

Jurisdictional Cost Apportionment

Appalachian continues to object to a step in jurisdictional cost apportionment which assigns a small portion of its costs to its short-term, limited-term and unit-power sales which were served during the test year as part of the annual and peak requirements. Appalachian wants to credit the revenues from these FPC jurisdictional sales to its cost of service, in similar fashion as was done relative with net revenues from affiliates under the Capacity Equalization Agreement. We could have used this method but we exercised our discretion to use a cost apportionment

method based on *actual test year and peak hour usage* by the short-term, limited-term and unit-power customers.

We thoroughly discussed Appalachian's contentions on this issue in our order of May 6, 1977, except for Appalachian's new argument that

> ". . . on January 17, *1977*, the date of maximum demand on Appalachian's and AEP's systems this past winter, neither Appalachian nor American Electric Power made any short-term or limited-term sales."

Again, this is an indirect attempt by Appalachian to shift from a *1974* test year to one that would include January *1977*. In the context of a new rate case based on a new set of complicated circumstances, the method approved by the Commission would still be one of several valid methods of cost apportionment. In a test year, including a January 17, 1977 peak, under the method approved in this Case No. 8182, the short-term and limited-term customers would *not* be assigned a portion of Appalachian's *demand* costs if they took no power during the peak hour, but they would be the *commodity* costs on the basis of allocation factors determined from test year sales to them. However, in that next rate case we will look at *Appalachian's capacity* situation and if it has or soon anticipates increased capacity from its 1301 Project at New Haven, West Virginia, we may adopt a different method of cost apportionment, such as the Average and Excess Demand method which we ordered to be filed by ordering paragraph 7 of our order dated May 6, 1977.

We adhere to our findings and conclusions on this issue as set forth in our said final order.

Third-Tier Rates

Appalachian requests the Commission to establish higher *Third-Tier* rates to be effective on and after May 1, 1977. As a basis for this request it argues that its costs of (1) coal, (2) labor, and (3) pollution control facilities are presently escalating over the cost increase adjustments we allowed in determining First-Tier rates for August 28, 1975, through April 30, 1976, and Second-Tier rates for May 1, 1976, through April 30, 1977.

Putting this request in perspective, we reiterate that the test year selected by the Company for Case No. 8182 was *1974*; unaudited *1975* data was received in evidence as an aid to assure ourselves of the reasonableness of our adjustments to 1974 test year data. The evidentiary hearings closed August 31, *1976*. We adopted the rare technique of establishing two sets of rates to be effective on and after two dates, because of the passage of time since the filed rates went into effect on August 28, 1975, and the date of our final order of May 6, 1977.

Appalachian now wants us to set higher rates in this Case No. 8182, for the period beginning May 1, 1977, on the basis of three cost component changes out of the multitude of revenue and cost changes that have occurred and are occurring as of July 1977.

We refuse to exercise our discretion to grant this request for many reasons, chief among which is that (1) the West Virginia customers of Appalachian deserve a modicum of rate stability, even if confined to the statutory lag period built in to our controlling statute, Code 24-2-4, and (2) the purported increased costs relied upon relate to the time periods too far beyond the end of the test period of 1974 to be the basis of a rate adjustment without entertaining a new test period study.

Appalachian recites increased fuel costs as a reason for higher Third-Tier rates. However, this ignores our caution at page 11 of our order issued May 6, 1977 that Appalachian "may be made to absorb any unreasonable differential between the price it pays for coal to its affiliated suppliers and to its non-affiliated coal producers". This is an issue

to be resolved in the future. Moreover, in monitoring monthly fuel costs of Appalachian's John Amos plant we have noted wide variations between the percentages ownership of the plant and the percentage of current monthly fuel purchases assigned to Appalachian. For example, for the fifteen-month period December 1976 through April 1977, the "swings" are as follows:

	Appalachian's Ownership Percentage	Appalachian's Fuel Cost Percentage	Differential
December 1976	69.735%	88.027%	18.292%
March 1977	65.550%	51.454%	(14.135%)

These circumstances raise substantial questions that are not susceptible to a *Third-Tier* rate solution in this Case No. 8182.

End Result

Even though our order issued May 6, 1977, balanced the various contentions according to sound regulatory principles and set Two-Tier rates on the basis of a 9.35% rate of return on rate base, Appalachian contends the rates set are too low.

Appalachian's argument rests on two misconceptions. First, it argues that its unaudited and unilateral view of its interest coverage as of March 31, 1977 is 1.99 times (199%) "eliminates Appalachian's legal ability to issue new mortgage bonds or debentures", because the issuance of such new debt requires at least 2.00 times (200%) interest coverage "for 12 consecutive months in the 15-month period immediately prior to the month in which the new debt securities are to be issued."

Second, Appalachian argues that a 9.35% *rate of return on rate base* "implies a return on common equity of but 12.8%", which, it contends, is too low on the evidence of *cost of capital on certain period-ended over-all capitalizations.*

These arguments are rejected as being based upon an unduly narrow view of the facts concerning interest coverage and a misconception of the relationship between the concept of *rate of return on rate base* in ratemaking and the concept of *cost of capital on capitalization* resulting from operations of a fiscal period.

The "interest coverage" test required to raise new debt funds from investors is *not* a test of "confiscation" in deciding whether rates are just and reasonable. The test is no more than a security device used to restrain a company from imprudent future debt financing. As the Commission said in *The Potomac Edison Company, Case No. 8280,* order issued April 25, 1977,

> "The Commission has not accepted and does not accept the proposition that the calculation of an interest coverage ratio and the resulting revenues requirement is a replacement for sound regulatory discretion. The revenue requirement to maintain any coverage ratio is greatly affected by changes in capital structure elemental components. The determination of what capital structure is appropriate for a utility has historically been left to management, and the Commission does not understand the Respondent as recommending otherwise. Therefore, we cannot accept the maintenance of a coverage ratio as a governing factor in ratemaking."

However, even if the "interest coverage" test was considered as an element in determining whether rates were or were not "just and reasonable", Appalachian's argument relying on *its* view of interest coverage on March 31, 1977, is not persuasive. Appalachian's earliest future debt financing would be late summer or early fall 1977. Any fifteen months period immediately prior to the month in which the new debt securities are to be issued, will include increased sales volumes, increased sales revenues due to growth and due to rate increases granted late in June 1977

by the FPC in its Docket No. ER77-325 and sought by Appalachian from the State Corporation Commission of Virginia through current hearings.

Moreover, Appalachian sought and secured approval for higher rates from this Commission on a 1974 test year having rate base costs and cost of service expenses relating to its Cabin Creek generating plant which is the subject of litigation before us and before the Federal courts. Whether or not this Commission prevails in its attempt to prevent Appalachian from prematurely discontinuing this plant from availability for service this coming winter or beyond, there appears to be no question that Appalachian will be able to reduce its costs associated with the Cabin Creek plant below the costs incurred during the test year 1974. To quantify this cost impact we will require Appalachian to provide this Commission with such data as an additional condition to our final order herein.

Finally, Appalachian's confusion in treating *cost of capital on end-of-period capitalization* as a strict determinant of *rate of return on rate base* in ratemaking has been thoroughly discussed at pages 22-25 of our final order herein. See also our discussion in *Hope Natural Gas Company, Case No. 8282,* order issued July 27, 1977, at pages 31-36.

We adhere to our belief that the "end result" of the rates we determined for Appalachian in our order issued May 6, 1977, are eminently just and reasonable.

Modification of Ordering Paragraphs 4 and 5

Appalachian requests that ordering paragraph of our order issued May 6, 1977, be modified to permit Appalachian to file revised tariff sheets 15 days "after final determination on the relief requested in this Petition", instead of 15 days from May 7, 1977. By filing its Petition for Rehearing, etc., seeking modification of ordering paragraph

4, Appalachian effectively tolled the running of the 15 days. We will modify our ordering paragraph 4, to require compliance on or before August 15, 1977.

Applicant requests that ordering paragraph 5 of our final order be modified to permit Appalachian to complete refunds within 60 days from the date such revised tariff sheets are finally approved. For similar reasons, we will modify our ordering paragraph 5 to require refunds to be complete within 60 days after our approval of the revised tariff sheets to be filed pursuant to this order and our order issued May 6, 1977. This means that if Appalachian files the revised tariff sheets on August 15, 1977, and we issue our order the same day approving same, that refunds will be required to be completed on or before October 14, 1977, unless our orders are stayed by a tribunal having jurisdiction so to do.

Clarifications

As additional guidance to incidental items not specifically mentioned in our order issued May 6, 1977, certain additional changes in the filed tariff sheets of W. Va. P.S.C. Tariff No. 3 are required as just and reasonable, consistent with our order, the record made and our recently effective "Rules and Regulations for the Government of Electric Utilities, 1977" as follows:

1. *Original Sheet No. 3-2*—Delete the last paragraph pertaining to a $2.00 or $10.50 service charge as not supported in the record by cost evidence, and see Electric Rule 5.06.

2. *Original Sheet No. 5-1, et al*—In the paragraph on "Equipment Supplied by Customer", change "$0.19" to "$0.17" per KW of monthly billing demand. Make the same adjustment in other schedules where applicable.

3. *Original Sheet No. 7-1, et al*—In the paragraph on "Equipment Supplied by Customer", change

"$0.32" to "$0.28" per KW of monthly billing demand. Make the same adjustment in other schedules where applicable.

4. *Original Sheet No. 10-1*—In the paragraph on "Adjustment of Demand Charge", modify "$0.00147" *to* "$0.00128 per KW of monthly billing demand [etc.]" for the period August 28, 1975, through April 30, 1976, and *to* "$0.00133 per KW of monthly billing demand, [etc.]" for the period May 1, 1976 forward.

5. *Original Sheet Nos. 5-1, 6-2, 7-2, 14 and 15*—Modify the "Payment" paragraph to change "fifteen (15)" to "twenty (20)" days and add a sentence "This delayed payment charge is not interest and is only to be collected once for each bill where appropriate."

6. *Original Sheet Nos. 8-2, 9-2, and 10-2*—Modify the "Payment" paragraph to change "fifteen (15)" to "twenty (20)" days, and change the last clause to read ". . . , customer shall pay Company a delayed payment charge on the total amount billed of 5% (but not less than $0.15). This delayed payment charge is not interest, and is only to be collected once for each bill when appropriate."

7. *Original Sheet Nos. 11-1, 16 and 17*—Modify the "Payment" paragraph to change "fifteen (15)" to "twenty (20)" days.

ORDER

A. The Commission denies Appalachian's request to reopen the evidentiary record, except that the Commission has fully considered the affidavits submitted by Appalachian with its Petition.

B. The Commission orders that paragraph 4 of its order issued May 6, 1977, be revised to extend the time to August 15, 1977, on or before which Appalachian shall file its revised tariff sheets in compliance with this order and our order issued May 6, 1977.

C. The Commission orders that paragraph 5 of its order issued May 6, 1977, be revised to extend the time for

Appalachian to complete its refunds within 60 days after the Commission's approval of the revised tariff sheets required to be filed by August 15, 1977.

D. The Commission hereby adds an ordering paragraph 8, to provide as follows:

8. Appalachian is hereby ordered to file on or before September 15, 1977, cost data for test year 1974 that would pertain both to rate base and over-all cost of service allocated to West Virginia which would be deducted if the Cabin Creek plant had not been in service during the test period 1974.

E. The Commission denies Appalachian's request to determine Third-Tier rates effective May 1, 1977, in this Case No. 8182, and

F. The Commission hereby affirms, as modified herein, its final order issued May 6, 1977.

s/ BROOKS E. SMITH
Chairman

PUBLIC SERVICE COMMISSION
OF WEST VIRGINIA

CHARLESTON

At a session of the PUBLIC SERVICE COMMISION OF WEST VIRGINIA, at the Capitol in the City of Charleston on the 26th day of August, 1977.

CASE No. 8182

APPALACHIAN POWER COMPANY, a corporation.
In the matter of increased rates and charges.

WHEREAS, by order entered herein on July 29, 1977, the Commission denied in part and granted in part a petition filed May 16, 1977, for rehearing, reopening of the record, reargument, and clarification of its order issued May 6, 1977; and

WHEREAS, upon due consideration and goods [sic] reasons appearing therefor, the Commission is of opinion and finds that this case should be reopened, set for further evidentiary hearing, and reargument in order to enable the Commission to determine the reasonableness of a third tier rate level increase effective May 1, 1977, on the basis of respondent's purported increases in cost of coal.

IT IS, THEREFORE, ORDERED that this matter be, and it hereby is reopened for further evidentiary hearing for the reason and purpose as above stated, and it is hereby set for further hearing to be held in the Commission's Hearing Room at the Capitol in the City of Charleston on the 27th day of October, 1977, at 9:30 a.m., EDT, at which time and place the respondent shall appear and prosecute its interests herein, and anyone interested may appear and make such objections thereto as may be deemed proper.

IT IS FURTHER ORDERED that the Secretary of the Commission give notice of this proceeding to all parties of record by mailing to each of them a copy of this order by United States Certified Mail, return receipt requested.

Chairman McDonald, deeming himself disqualified, took no part in the consideration or decision of this matter.

A COPY.

TESTE:

s/ S. Grover Smith, Jr.
S. GROVER SMITH, JR.,
Secretary

PUBLIC SERVICE COMMISSION OF WEST VIRGINIA

CHARLESTON

At a session of the PUBLIC SERVICE COMMISSION OF WEST VIRGINIA at the Capitol in the City of Charleston on the 30th day of August, 1977.

CASE No. 8182

APPALACHIAN POWER COMPANY, a corporation.
In the matter of increased rates and charges.

By Commission order entered herein on July 29, 1977, Appalachian Power Company, a corporation, was ordered to file Revised Tariff Sheets by August 16, 1977 in compliance with our Order issued May 6, 1977 and our Order issued July 29, 1977. The Tariff Sheets to be effective August 28, 1975, through April 30, 1976, were to reflect rates and charges set forth in Appendix F of our Order of May 6, 1977, which rates and charges were sufficient to recover an additional $15,380,249 over the annual revenue level produced by rates which were in effect prior to August 28, 1975. The Tariff Schedules to be effective on and after May 1, 1976, were to reflect rates and charges specified in Appendix F of our Order of May 6, 1977, which rates and charges were sufficient to recover an additional $20,309,899 over the annual revenue level produced by rates which were in effect prior to August 28, 1975.

On August 15, 1977, Appalachian did submit to the Commission, Original Sheets or its P.S.C. W.Va. Tariff No. 3, cancelling its P.S.C. W.Va. Tariff No. 2, effective August 28, 1975 through April 30, 1976. Likewise, on August 15, 1977, Appalachian filed First Revisions of Original Sheets of its P.S.C. W.Va. Tariff No. 3, for service on and after May 1, 1976. The Tariffs were inspected by the Commission and were found to be generally in compliance with our

Orders of May 6, 1977 and July 29, 1977, except in the following instances:

(1) *Original Sheet No. 3-6 and First Revision of Original Sheet No. 3-6.*

Use of Energy by Customer

The paragraph beginning, "the customer shall install . . ." is not in compliance with the requirements of our Order dated May 6, 1977. This paragraph should be changed to read as follows:

> The customer shall install only motors, apparatus or appliances which are suitable for operation with the character of the service supplied by the Company, and which shall not be detrimental to same, and the electric power must not be used in such a manner as to cause unprovided for voltage fluctuation or disturbances in the Company's transmission or distribution system. While the Company may be the initial judge as to the suitability of apparatus or appliances, and also as to whether the operation of such apparatus or appliances is or will be, detrimental to its general service, the Public Service Commission of West Virginia shall be the proper forum for settling any disputes under this section which cannot be satisfactorily settled between the Company and its customer.

(2) *Original Sheet No. 3-6 and First Revision of Original Sheet No. 3-6.*

Domestic Service

The last sentence of the second paragraph should be changed to read as follows:

> Larger motors may be served when, in the Company's initial judgment, the existing service facilities of the Company are adequate; however, the Public Service Commission of West Virginia shall be the proper forum for settling any disputes under this section which cannot be satisfactorily settled between the Company and its customer.

(3) *Effective Dates*

The Tariff submitted by Appalachian for service on and after May 1, 1976, indicated that it was "Effective: October 1, 1977". The Commission finds this to be in error, and in view of our Order dated August 26, 1977 which reopens this case for limited purposes, such Tariff Schedules should be changed to read:

Effective: May 1, 1976 through April 30, 1977.

Except for the items pertaining to terms and conditions of service and effective dates of Tariffs, as hereinabove discussed, the Tariffs filed by Appalachian on August 15, 1977 are found to be in compliance with our Orders of May 6, 1977 and July 29, 1977.

It is Therefore, Ordered that the rates and charges set forth in the Tariffs submitted by the respondent on August 15, 1977, shall be placed in effect on the dates specified in the aforementioned Commission Order of May 6, 1977.

It is Further Ordered, that Appalachian shall file Revised Schedules reflecting the terms and conditions of service and effective dates hereinabove prescribed within ten (10) days of the date of this Order.

It is Further Ordered, that the sixty (60) day maximum period allowed to the respondent, Appalachian Power Company to complete its refunds to its customers as set forth in paragraph five of the "ORDER" section of our order of May 6, 1977, and paragraph C of the "ORDER" section of our order of July 29, 1977, shall begin to run as of the date of this order.

Chairman McDonald, deeming himself disqualified, took no part in the consideration or decision of this matter.

A Copy.

Teste:

s/ S. Grover Smith, Jr.
S. Grover Smith, Jr.
Secretary

STATE OF WEST VIRGINIA

At a Regular Term of the Supreme Court of Appeals continued and held at Charleston, Kanawha County, on the 10th day of October, 1977, the following order was made and entered, to-wit:

Appalachian Power Company, a corporation
vs.

The Public Service Commission of West Virginia

Upon an appeal from, suspension and review of the final order of the Public Service Commission of West Virginia made and entered on May 6, 1977, as revised, modified and affirmed by the Commission's Order issued on July 29, 1977.

The Court, having maturely considered the petition; amended petition; note of argument in support thereof; the record consisting of all papers, documents and evidence which were before the Public Service Commission at the hearing which resulted in the entry of the final order complained of; the statement of reasons for the entry of its order of the 6th day of May, 1977, as revised, modified and affirmed by the Commission's Order issued on July 29, 1977, filed herein by the respondent, Public Service Commission of West Virginia on October 3, 1977; and the oral argument of counsel on the 4th day of October, 1977, the date fixed by the Court for hearing upon the aforesaid petitions; is of opinion that the petitioner has not shown itself entitled to the relief prayed for in its said petition. It is therefore considered and ordered that the prayer of the petition for an appeal from, suspension and review, in this proceeding, be, and the same is hereby, denied. Justice Miller would grant.

It is further ordered that leave be, and the same is hereby, granted to the Public Service Commission of West

Virginia to withdraw from the office of the Clerk of this Court, the record consisting of all papers, documents and evidence originally filed with the Public Service Commission of West Virginia.

A True Copy

Attest:

s/ GEORGE W. SINGLETON
Clerk Supreme Court of Appeals

IN THE
SUPREME COURT OF APPEALS OF
WEST VIRGINIA

CHARLESTON

APPALACHIAN POWER COMPANY, a corporation,
Appellant,

v. (P.S.C. Case No. 8182) No.

PUBLIC SERVICE COMMISSION OF WEST VIRGINIA,
Appellee.

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

Notice is hereby given that Appalachian Power Company, the appellant above named, hereby appeals to the Supreme Court of the United States from the final order of the Supreme Court of Appeals of the State of West Virginia entered in this proceeding on October 10, 1977, which denied Appalachian Power Company's Petition for an appeal from, and review of, the order of the Public Service Commission of West Virginia, the appellee above named, of May 6, 1977, as revised, modified and affirmed by its orders of July 29 and August 30, 1977.

This appeal is taken pursuant to 28 U.S.C. § 1257(2).

Dated: October 14, 1977.

s/ CHARLES R. MCELWEE

.....

Counsel for Appalachian Power
Company, Appellant

Received
1977 Oct 14 PM 3:19
Public Service Commission of W. Va.
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Charleston, West Virginia 25323

Attorneys for Appellant,
Appalachian Power Company

AFFIDAVIT OF SERVICE OF NOTICE OF APPEAL

State of West Virginia,
County of Kanawha, To Wit:

I, Charles R. McElwee, an attorney in the office of Love, Wise, Robinson & Woodroe, attorneys of record for Appalachian Power Company, appellant herein, depose and say that on the 14th day of October, 1977, I served a copy of the foregoing Notice of Appeal to the Supreme Court of the United States upon the Public Service Commission of West Virginia, appellee herein, by delivering the same to Arnold Weiford and C. Terry Owen, counsel of record for said Public Service Commission of West Virginia, at their offices in the State Capitol, Charleston, West Virginia; and upon Appalachian Research & Defense Fund, Inc., Mercer County Economic Opportunity Corporation, and McDowell County Consumer Action Council, Inc., Intervenors in P.S.C. Case No. 8182, by delivering the same to Robert R. Rodecker, counsel of record for said Intervenors, at his office located at 1116-B Kanawha Boulevard, East, Charleston, West Virginia 25301; and upon the City of Charleston and the City of South Charleston, Intervenors in P.S.C. Case No. 8182, by delivering the same to Vincent V. Chaney and Michael T. Chaney, counsel of record for said Intervenors, at their office located at 1616 Charleston National Plaza, Charleston, West Virginia 25301; and upon FMC Corporation, Intervenor in P.S.C. Case No. 8182, by delivering the same to T. D. Kauffelt, counsel of record for said Intervenor, at his office located at 803 Kanawha Valley Building, Charleston, West Virginia 25301; and upon ACF Industries, Inc., American National Rubber Company, Houdaille Industries, Inc., Huntington Alloys, Inc., Chemetron Corporation and

Owen-Illinois, Inc., Intervenors in P.S.C. Case No. 8182, by delivering the same to John C. Lobert and C. E. Goodwin, counsel of record for said Intervenors, at their office located at 1717 Charleston National Plaza, Charleston, West Virginia 25301; and upon Mrs. Lucille Gillespie, Protestant in P.S.C. Case No. 8182, by depositing the same in the United States mailbox, with first class postage prepaid, addressed to her at Post Office Box 44, Clendenin, West Virginia 25045.

s/ CHARLES MCELWEE
Charles McElwee

Subscribed and sworn to before me, s/ Mary N. Staples, at Charleston, West Virginia, this 14th day of October, 1977.

s/ MARY N. STAPLES
Notary Public in and for
Kanawha County, West Virginia

My commission expires June 6, 1985.

PUBLIC SERVICE COMMISSION
OF WEST VIRGINIA

CHARLESTON

APPALACHIAN POWER COMPANY, a corporation,
Appellant,

v. (P.S.C. Case No. 8182) No.

PUBLIC SERVICE COMMISSION OF WEST VIRGINIA,
Appellee.

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

The petition to the Commission for rehearing of its final order of May 6, 1977 having been denied in part by the Commission's order of July 29, 1977, and the petition to the West Virginia Supreme Court of Appeals for appeal from the Commission's May 6, 1977 order, as revised, modified and affirmed, having been denied by the West Virginia Supreme Court of Appeals' order of October 10, 1977.

Notice is hereby given that Appalachian Power Company, the Appellant above named, hereby appeals to the Supreme Court of the United States from the order issued in this proceeding by the Public Service Commission of West Virginia, the Appellee above named, on July 29, 1977, to the extent that such order, as revised, modified and affirmed by its orders of August 26 and August 30, 1977, denied Appellant the relief sought in its petition for rehearing of Appellee's order of May 6, 1977.

Received
1978 Jan 3 PM 4:39
Public Service Commission of W. Va.
Secretary's Office

This appeal is taken pursuant to 28 U.S.C. §1257(2).

Dated: January 3, 1978

s/ CHARLES R. McELWEE

Attorney for Appalachian Power Company, Appellant

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Attorneys for Appellant,
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AFFIDAVIT OF SERVICE OF NOTICE OF APPEAL

STATE OF WEST VIRGINIA,
COUNTY OF KANAWHA, TO WIT:

I, Charles R. McElwee, an attorney in the office of Love, Wise, Robinson & Woodroe, attorneys for Appalachian Power Company, appellant herein, depose and say that on the 3rd day of January, 1978, I served a copy of the foregoing Notice of Appeal to the Supreme Court of the United States upon the following persons by depositing the same in a United States mailbox, first class postage prepaid, addressed to counsel of record as indicated:

Person(s)	*Counsel of Record*
The Public Service Commission of West Virginia, Appellee	Arnold Weiford, Esq. C. Terry Owen, Esq. The Public Service Commission of West Virginia State Capitol Charleston, West Virginia 25301
Appalachian Research & Defense Fund, Inc., Mercer County Economic Opportunity Corporation and McDowell County Consumer Action Council, Inc., Intervenors	Robert R. Rodecker, Esq. 1116-B Kanawha Blvd., East Charleston, West Virginia 25301
The City of Charleston and the City of South Charleston, Intervenors	Vincent V. Chaney, Esq. Michael T. Chaney, Esq. 1616 Charleston National Plaza Charleston, West Virginia 25301
FMC Corporation, Intervenor	T. D. Kauffelt, Esq. 803 Kanawha Valley Building Charleston, West Virginia 25301
ACF Industries, Inc., American National Rubber Company, Houdaille Industries, Inc., Huntington Alloys, Inc., Chemetron Corporation and Owen-Illinois, Inc., Intervenors	John C. Lobert, Esq. C. E. Goodwin, Esq. 1717 Charleston National Plaza Charleston, West Virginia 25301

Supreme Court, U. S.
FILED
FEB 8 1978
MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

October Term, 1977

No. 77-979

Appalachian Power Company,
Appellant,

v.

The Public Service Commission of West Virginia,
Appellee.

ON APPEAL FROM THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

MOTION TO DISMISS OR AFFIRM

Arnold O. Weiford, *General Counsel*
Clement R. Bassett
George Zivkovich
C. Terry Owen
Attorneys for Appellee

E-214 State Capitol Building
Charleston, West Virginia 25305

February 8, 1978

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IN THE

Supreme Court of the United States

October Term, 1977

No. 77-979

APPALACHIAN POWER COMPANY,
Appellant,

v.

THE PUBLIC SERVICE COMMISSION OF WEST VIRGINIA,
Appellee.

ON APPEAL FROM THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

MOTION TO DISMISS OR AFFIRM

Appellee, The Public Service Commission of West Virginia, pursuant to Rule 16 of the Rules of the Supreme Court of the United States, moves the Court to dismiss the appeal herein or in the alternative to affirm the judgment of the Supreme Court of Appeals of West Virginia on the grounds that it does not present a substantial federal question.

NATURE OF THE CASE AND PROCEEDINGS BELOW

On March 31, 1975, Appalachian Power Company (hereinafter "Appalachian" or "company") an electric public utility corporation operating in West Virginia, filed with the Public Service Commission of West Virginia (hereinafter "Commission"), pursuant to Chapter 24, Article 2, Section 4 of the West Virginia Code, 1931, as amended, (hereinafter "Code"), its tariff designated P.S.C. W.Va. No. 3, cancelling P.S.C. W.Va. No. 2, stating increased rates and charges for electric service in the territory served by it in West Virginia, to become effective May 1, 1975.

The filed rates would have increased rates about $40 Million annually; the test year was calendar 1974; and the Commission Case Number is 8182.

The Commission, by order of April 4, 1975, suspended the tariff filing and deferred the use of the rates and charges stated therein until August 28, 1975, at which time the rates became effective under bond, and subject to refund.

Evidentiary hearings were held by the Commission on sixteen days, beginning July 21, 1975, and ending August 31, 1976. The transcript of testimony contains 2,515 pages. Additional quantities of pre-filed testimony and exhibits are also in the file. Briefs were filed, and the last brief was filed November 9, 1976.

On May 6, 1977, the Commission entered its "Final Order" in Case No. 8182. (See Appendix, page B-1). The company filed a Petition for Rehearing, Reopening and Reargument, and the Petition was granted in part and denied in part by Commission order entered July 29, 1977. (Please see Appendix, page D-1). Other Commission

orders of August 26, 1977, and August 30, 1977, among other items stated therein, set the matter of rates from May 1, 1977, forward for further hearing which was held on October 27, 1977. (Please see Appendix, pages E-1 and F-1). An order of the Commission entered on January 13, 1978, established rates beginning May 1, 1977. (Please see Appendix, Page G-1).

It should be noted that the previous Commission orders had established rates for the first two of three periods ("tiers"); one, from August 28, 1975, through April 30, 1976; two, from May 1, 1976 through April 30, 1977; and the third of three periods being from May 1, 1977, until presumably March 1978.

In the meantime, on *September 12, 1977,* Appalachian filed a *new* tariff (P.S.C. W.Va. No. 4) increasing rates and charges approximately $85 Million annually, which the Commission suspended for 120 days beyond November 14, 1977. Hearings on this new matter (Commission Case No. 9091) began January 16, 1978, and further proceedings are scheduled in January and February, 1978.

On August 26, 1977, Appalachian petitioned the Supreme Court of Appeals of West Virginia (hereinafter "West Virginia Court") for review of Commission orders of May 6, 1977, and July 29, 1977. Appalachian raised a number of issues including West Virginia Constitutional issues, and United States Constitutional issues.

At issue before the West Virginia Court were rates of tiers one and two, from August 25, 1975 through April 30, 1977.

On October 10, 1977, the West Virginia Court, entered its order denying the Petition of Appalachian for Review (Please see Appendix, page A-1).

On October 14, 1977, Appalachian filed its Notice of Appeal to this Court. A stay of Commission orders was granted by The Honorable Chief Justice Warren E. Burger.

Appalachian filed its Jurisdictional Statement herein on January 7, 1978 (dated January 6, 1978 and received by Appellee January 9, 1978) and this Brief attached to Appellee's Motion to Dismiss or Affirm and filed therewith (Rule 35, Paragraph 1, Rules of the Supreme Court of the United States) is hereby submitted in opposition to Appalachian's appeal, and in support of the appellee's Motion to Dismiss the appeal or in the alternative to affirm the judgment of the West Virginia Court.

ARGUMENT — INTRODUCTION

This is a case based on public utility ratemaking by a state commission. The appellant, Appalachian, alleges unconstitutional "confiscation" of property, and further alleges a burden upon or interference with interstate commerce.

Both of appellant's contentions are without merit.

The appellant in its Jurisdictional Statement, pyramids a series of assumptions to support its case. It assumes that the regulatory commission has a responsibility to insure net earnings twice the amount of the interest owed, and that if it does not, this amounts to confiscation and a burden upon interstate commerce.

We will demonstrate below not only the invalidity of the proposition that coverage of 2.0 times should be a critical test in ratemaking, but also that Appalachian has by its own actions manipulated its financial data so as to make it appear that its coverage is lower than it is.

We will also demonstrate that case law, federal and state, holds that confiscation in ratemaking does not include as confiscation the failure to meet a 2.0 times coverage test, of net earnings over interest owed.

Also, we refute the contention that the Commission failed to consider Appalachian's capital attraction requirements in Case No. 8182.

All of which, when reviewed and studied, will lead to the conclusion that there is no merit to this appeal, that the net result of the appeal has been to obtain a stay of refunds for several months beyond October 1977, when ordered to be made, all pending the imposition of higher rates under bond in a *new* rate case in March of 1978.

Our Argument is contained in six parts as follows:

I. FAILURE TO ATTAIN A CERTAIN "COVERAGE" IS NOT "CONFISCATION" IN THE CONSTITUTIONAL SENSE: AND, THEREFORE, IS NOT A VIOLATION OF THE FIFTH AND FOURTEENTH AMENDMENTS OF THE UNITED STATES CONSTITUTION.

II. THE WEST VIRGINIA PUBLIC SERVICE COMMISSION DID CONSIDER APPALACHIAN'S CAPITAL ATTRACTION REQUIREMENTS IN ITS ORDERS OF MAY 6, 1977, AND JULY 29, 1977.

III. "COVERAGE" REQUIREMENTS IN PUBLIC UTILITY RATEMAKING.

A. WHY THE USE OF A "COVERAGE" REQUIREMENT AS A "CRITICAL TEST" OF

CONFISCATORY RATES IN PUBLIC UTILITY RATEMAKING IS UNSOUND, UNRELIABLE, AND JUST PLAIN WRONG.

B. COMMENTS ON EXACTLY HOW 2.0 TIMES COVERAGE AFFECTS EQUITY LEVELS.

IV. AS A MATTER OF FACT, WHAT IS APPALACHIAN'S FIRST MORTGAGE BOND "COVERAGE" IN 1977?

V. SOME COMMENTS ON APPALACHIAN'S CREDIT STANDING.

VI. THE COMMISSION ORDERS DO NOT UNCONSTITUTIONALLY BURDEN OR INTERFERE WITH INTERSTATE COMMERCE.

ARGUMENT

I. FAILURE TO ATTAIN A CERTAIN "COVERAGE" IS NOT "CONFISCATION" IN THE CONSTITUTIONAL SENSE; AND THEREFORE, IS NOT A VIOLATION OF THE FIFTH AND FOURTEENTH AMENDMENTS OF THE UNITED STATES CONSTITUTION.

Confiscation as used in public utility ratemaking, has been defined for many years by numerous courts, federal and state. To have "confiscation" the rates established by the ratemaking authority must be so low as to amount to a deprivation of property without just compensation. The rates must be below the "floor of confiscation." Between this floor of confiscation and the "ceiling of excessiveness" there is a broad range of reasonable and fair rates, over which reasonable men may differ, but which the courts have repeatedly held to be the duty of ratemaking bodies to establish.

The reasonable or fair return which the public utility realizes is a return over and above legitimate operating expenses, depreciation, and taxes. Nowhere in this formula have the courts ever said that the only reasonable or fair return is one which gives net earnings equal to two times or more the amount of interest owed.

There are numerous reasons why to say so would be unsound. Herewith follows our argument as supported by case law.

As stated above, "confiscation" in public utility ratemaking, to be in violation of the Fifth and Fourteenth Amendments of United States Constitution, must be of such a character as to amount to a deprivation of property without just compensation, or without due process of law.

San Diego Land & Town Co. v. *National City* 174 U.S. 739, 19 S.Ct. 804, 43 L.Ed. 1154 (1899).

Board of Public Utility Commissioners v. *New York Telephone Co.* 271 U.S. 23, 46 S.Ct. 363, 70 L.Ed. 808 (1926).

Denver Union Stock Yard Co. v. *United States,* 304 U.S. 470, 58 S.Ct. 990, 82 L.Ed. 1469 (1938).

The "fair" return, or "reasonable" return which makes up the "just compensation" is upon the value of the property *used* at the time that it *is rendering* public service.

Denver Union Stock Yard Co. v. *United States,* supra.

Board of Public Utility Commissioners v. *New York Telephone Co.*, supra.

Bluefield Water Works & Improvement Company v. *Public Service Commission,* 262 U.S. 679, 43 S.Ct. 675, 67 L.Ed. 1176 (1923).

McCardle v. *Indianapolis Water Co.*, 272 U.S. 400, 47 S.Ct. 144, 71 L.Ed. 316 (1927).

This principle: that the fair return must be on property *used* and *useful* in furnishing public utility service at the time the service is being furnished is also the law in West Virginia, as announced by its State Supreme Court.

In *Pittsburgh & West Virginia Glass Co.* v. *The Public Service Commission of West Virginia*, 101 W.Va. 63, 132 S.E. 497 (1926), the West Virginia Supreme Court, after stating that a Commission order fixing rates will not be disturbed unless the finding of fact is contrary to the evidence, or without evidence to support it, or there is a misapplication of legal principles; and after saying that probative value accorded by the Commission on substantial conflict of evidence will not be disturbed; the Court then states in Headnote No. 2, 101 W.Va. 64:

> "Rates — Burden of Proving a Rate to be Confiscatory is on Public Utility and Unless Evidence is Clear That Rate is Too Low to Afford Reasonable Return on Value of Property Order Fixing it Will Not be Disturbed.
>
> When a rate fixed by the Commission is attacked as confiscatory, the burden of proving it to be so is upon the public utility, and unless the evidence is clear that the rate is too low to afford a reasonable return on the value of the property used and useful in the service of the public the order fixing the rate will not be disturbed. (p. 67)"

Appellant contends that failure to meet a 2.0 times coverage test for net earnings is constitutional "confiscation."

This contention on its face does *not* meet the test or standard of constitutional confiscation set by this Court nor that set by the West Virginia Supreme Court.

In the case before this Court, the Commission granted a Rate of Return of *9.35%* which on a Rate Base of $488,976,907, being the value of the property of Appalachian *used* and *useful* in rendering electric service to West Virginia customers, amounts to an overall return of about $46,000,000 annually from the company's West Virginia operations alone. The annual rate of return of 9.35% includes an imputed return on equity of *12.8%*.

The Courts are not given powers to make rates or fix rates; and should inquire concerning results in order to uphold the constitutional guarantees against the taking of property without just compensation.

> *Mitchell Coal & Coke Co.* v. *Pennsylvania R. Co.* 230 U.S. 247, 33 S.Ct. 916, 57 L.Ed. 1472 (1913).
>
> *Pacific Gas & Electric Co.* v. *San Francisco* 265 U.S. 403, 44 S.Ct. 537, 68 L.Ed. 1075 (1924).
>
> *San Diego Land & Town Co.* v. *National City*, supra.

We submit in all seriousness that there is *no* deprivation of property without just compensation in this case when the Commission has granted a 9.35% Rate of Return on property used and useful in rendering electric service. Further Appalachian is unable to show that it has been deprived of any title, right, privilege or immunity protected by the Constitution.

The $46,000,000 annual return to Appalachian is well up and quite high in the "zone of reasonableness" contemplated by this Court, within which it will not set aside rates that produce such a return. If within this "zone of reasonableness" then such rates cannot be said to be unjust and unreasonable; and if the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry is at an end.

Mobil Oil Corp. v. *Federal Power Commission* 417 U.S. 283, 94 S.Ct. 2328, 41 L.Ed. 2d 72 (1974).

If the rate order cannot be said to be unjust and unreasonable, then the Court is not further obliged to examine every detail of the rate order, and it is then not important that the method employed to reach the result may contain infirmities.

Mobil Oil Corp. v. *Federal Power Commission*, supra.

Federal Power Commission v. *Hope Natural Gas Co.* 320 U.S. 591, 64 S.Ct. 281, 88 L.Ed. 333 (1944).

Appalachian's whole case rests upon establishing "confiscation" of such a nature as to amount to a deprivation of *property* by the Commission *without just compensation.*

This, Appalachian has not done and cannot do and the appeal must fail at this point.

Rates which allow a return of *$46,000,000* annually over and above *all* operating expenses, depreciation, and taxes, just simply are not a deprivation of property.

Within this "Zone of reasonableness" the determination of what is a reasonable rate for a public utility is a legislative responsibility (of the Commission) and not a judicial question for the Courts. Conclusions may differ as to what exactly is a fair return for a public utility. There is no exact rate which a public utility subject to legislative control can say that it has a "right" to obtain.

Munn v. *Illinois* 94 U.S. 113, 24 L.Ed. 77 (1876).

United Railways & Electric Co. v. *West*, 280 U.S. 234, 50 S.Ct. 123, 74 L.Ed. 390. (1930).

Willcox v. *Consolidated Gas Co.*, 212 U.S. 19, 29 S.Ct. 192, 53 L.Ed. 382 (1909).

Appalachian wishes to extend the threshold of the "zone of reasonableness" another $20,000,000 annually and this wish is not consistent with the law and not supported by the case law cited above and numerous other cases.

What then, is it that Appalachian wants? It wants to establish that *net earnings* before interest expense must, as a matter of constitutional law, be *twice* the amount of the interest owed by Appalachian, no matter what the amount of the debt.

Below in a separate section we will demonstrate, and we hope convincingly, why coverage of 2.0 times should not be a critical test of "confiscation" in ratemaking.

At this point it will suffice to say that no Court in this Nation at any Judicial level: Federal, State or Local has ever held that 2.0 times "coverage" is such a critical test.

On the contrary, in many cases the Court has rejected the argument that rates must, as a matter of law, be high enough to guarantee a net earnings of twice the amount of interest owed.

Typical are a Virginia Supreme Court case and an Idaho Public Utilities Commission case, which we take the liberty of citing, not as controlling, but as indicative of the reasoning of Commissions and Courts, other than in West Virginia, who have considered Appalachian's contention.

In Virginia, its Supreme Court affirmed its "State Corporation Commission" (Public Utility) in an electric company case in January, 1976, where the Commission had found a rate of return of 8.40% and a calculated

return of 11.24% on common equity to be proper. The Court in its decision states:

> "Accordingly, from an examination of this entire record, we hold that the overall rate of return established in this case is within the 'reasonably wide area' of legislative discretion and is therefore not erroneous as a matter of law."
>
> "On this record, we cannot accept Appalachian's contention that the 'Commission's decision to establish an overall rate of return of 8.40% and a calculated return of 11.24% places the Company in a financial position whereby it cannot raise the additional capital necessary to discharge its statutory duties.' This is but a reassertion, in a different context, of the issues discussed in Part I of this opinion and required no additional elaboration.
>
> For the reasons assigned, the order of the Commission is *Affirmed.*"

The question posed to the Virginia Supreme Court was identical with the question before this Court:

> "Third, were the ordered rates unjust and unreasonable and an unconstitutional deprivation of property without due process of law, 'if the end result of the Commission's decision leaves Appalachian in a financial position in which it is unable to attract the capital necessary for the proper discharge of its public duties.' The answer to each question is in the negative and we affirm."
>
> *Appalachian Power Company* v. *Commonwealth of Virginia,* Supreme Court of Virginia, 221 S.E. 2d 872 (1976).

A recent Idaho Public Utility Commission case dealt with this question of coverage and arrived at the conclusion that the simple calculation of an interest coverage ratio and the resulting revenue requirement is *not* a replacement for *sound* regulatory discretion.

We quote:

> "We have not accepted and do not now accept the proposition that the simple calculation of an interest coverage ratio and the resulting revenue requirement is a replacement for sound regulatory discretion. The revenue requirement to maintain any coverage ratio is greatly affected by changes in capital structure elemental components. The determination of what capital structure is appropriate for a utility has historically been left to management, and we do not understand applicant as recommending otherwise. Therefore, we cannot accept the maintenance of a coverage ratio as a governing factor in ratemaking."
>
> Re *Washington Water Power Company,* Idaho Public Utilities Commission, 17 PUR 4th 70 (1976).

And this Commission (West Virginia) likewise has recognized the broad range of reasonableness in ratemaking when in a recent case it states:

> " . . . there is a great deal of leeway for decision on *over-all* rate of return by a regulatory body. The lower limit of a fair rate of return on rate base is set by the constitutional protection against "confiscation". The upper limit is likewise a judgment decision of what would be an "Excessive" rate of return in the circumstances of each case. There is a broad band of reasonable earnings or reasonable rates of return between the "floor of confiscation" and the "ceiling of excessiveness"."
>
> *Columbia Gas of West Virginia, Inc.,* Case No. 8807 Public Service Commission of West Virginia (June 14, 1977) (Unreported).

And, this Court has on occasion upheld the principle that the return on investment may, consistent with the United States Constitution, be limited stringently by rate regulation, and that the investors' interests provide only

one of the variables in the "constitutional calculus of reasonableness."

> *Permian Basin Area Rate Cases*, 390 U.S. 747, 88 S. Ct. 1344, 20 L.Ed. 2d 312 (1968).
>
> *Federal Power Commission* v. *Texaco, Inc.*, 417 U.S. 380 94 S.Ct. 2315, 41 L.Ed. 2d 141 (1974).

Appalachian relies heavily on *Bluefield Water Works & Improvement Company* v. *Public Service Commission*, supra, and *Federal Power Commission* v. *Hope Natural Gas Co.*, supra.

We quote "Headnote 5" of *Bluefield Water Works and Improvement Company* v. *Public Service Commission of West Virginia*, 262 U.S. 679, 67 L.Ed. 1176 (1923) (Emphasis ours).

> "5. A public utility is entitled to such rates as will permit it to earn a return upon the value of the property *which it employs for the convenience of the public* equal to what generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by *corresponding risks and uncertainties, but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures.*"

We note that *the property must be employed for the use of the public.* Also, one must realize that risk and uncertainty in regulated industry is less than unregulated industry. During periods of economic difficulty, utilities are assured an opportunity to earn a reasonable return on investment. Unregulated industry is not so assured. Appalachian would have the best of both worlds. It seeks to be assured of adequate earnings during periods of

economic difficulty, and an opportunity to make earnings comparable to unregulated industry during periods of economic bliss. The Court further found that there is no constitutional right to certain high "profits".

The United States Supreme Court adopts much of the above quoted principles and ideas in: *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591, 64 S.Ct. 281, 88 L.Ed. 333, 51 PUR (NS) 193, (1944) at pages 602 and 603 of *320 U.S.*, (Emphasis ours).

> "We held in Federal Power Commission v. Natural Gas Pipeline Co. *supra*, that the Commission was not bound to the use of any single formula or combination of formulae in determining rates.
>
> Its rate-making function, moreover, involves the making of "Pragmatic adjustments." Id. at p. 586. And when the Commission's order is challenged in the courts, the question is whether that order "viewed in its entirety" meets the requirements of the act. Id. at p. 586. Under the statutory standard of "just and reasonable" *it is the result reached, not the method employed, which is controlling.* Cf. Los Angeles Gas & E. Corp. v. California R. Commission, 289 U.S. 287, 304, 305, 314, 77. L.Ed. 1180, PUR 1933C 229, 53 S.Ct. 637; West Ohio Gas Co. v. Ohio Pub. Utilities Commission (1935) 294 U.S. 63, 70, 79 L.Ed. 761, 6 PUR (NS) 449, 55 S.Ct. 316; West v. Chesapeake & P. Teleph. Co. 295 U.S. 662, 692, 693, 79 L.Ed. 1640, 8 PUR (NS) 433, 55 S.Ct. 894 (dissenting opinion). It is not theory but the impact of the rate order which counts. *If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the act is at an end. The fact that the method employed to reach that result may contain infirmities is not then important. Moreover, the Commission's order does not become suspect by reason of the fact that it is challenged. It is the product of expert judgment which carries a pre-*

sumption of validity. And he who would upset the rate order under the act carries the heavy burden of making a convincing showing that it is invalid because it is unjust and unreasonable in its consequences. Cf. Railroad Commission v. Cumberland Teleph. & Teleg. Co. (1909) 212 U.S. 414, 53 L.Ed. 577, 29 S.Ct. 357; Lindheimer v. Illinois Bell Teleph. Co., *supra*, 292 U.S. at pp. 164, 169; California R. Commission v. Pacific Gas & E. Co. (1938) 302 U.S. 388, 401, 82 L.Ed. 319, 21 PUR (NS) 480, 58 S.Ct. 334.

The rate-making process under the act, i.e., the fixing of "just and reasonable" rates, involves a balancing of the investor and the consumer interests. Thus we stated in the Natural Gas Pipeline Company Case that *'regulation does not insure that the business shall produce net revenues.'* 315 U.S. at p. 590. But such considerations aside, the investor interest has a legitimate concern with the financial integrity of the company whose rates are being regulated. From the investor or company point of view it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business. These include service on the debt and dividends on the stock. Cf. Chicago & G.T.R. Co. v. Wellman (1892) 143 U.S. 339, 345, 346, 36 L.Ed. 176, 12 Ct. 400. By that standard the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and attract capital. See Missouri ex. rel. Southwestern Bell Telph. Co. v. Public Service Commission, 262 U.S. 276, 291, 67 L.Ed. 981, PUR 1923C 193, 43 S.Ct. 544, 31 ALR 807 (Mr. Justice Brandeis concurring). *The conditions under which more or less might be allowed are not important here. Nor is it important to this case to determine the various permissible ways in which any rate base on which the return is computed might be arrived at. For we are of the*

view that the end result in this case cannot be condemned under the act as unjust and unreasonable from the investor or company viewpoint.

The United States Supreme Court did *not* condemn the end result of the Federal Power Commission decision from the *investor* or company *viewpoint.*

And, in the same United States Supreme Court case *(Federal Power Commission* v. *Hope Natural Gas Co.)* the Court speaks out on what legal avenues are open to companies when the future discloses a negative situation: (Page 615 of *320 U.S.*)

> *"It is suggested that the Commission has failed to perform its duty under the Act in that it has not allowed a return for gas production that will be enough to induce private enterprise to perform completely and efficiently its functions for the public. The Commission, however, was not oblivious of those matters. It considered them . . . No serious attempt has been made here to show that they are inadequate. We certainly cannot say that they are, unless we are to substitute our opinions for the expert judgment of the administrators to whom Congress entrusted the decision. Moreover, if in light of experience they turn out to be inadequate for development of new sources of supply, the doors of the Commission are open for increased allowances. This is not an order for all time. The Act contains machinery for obtaining rate adjustments."*

Not only is the machinery available to Appalachian, indeed, it has availed itself of such machinery and on September 12, 1977, it filed a new set of rates, which will become effective under the law within 120 days of November 14, 1977. The company should not make a mockery of judicial processes by using otherwise legal avenues to gain new consideration on rates, and then to complain of being

deprived of its constitutional rights to have reasonable and just rates.

This Court in *Federal Power Commission* v. *Hope*, supra, while saying that the investor interest should be considered, also said that regulation does not insure that the business shall produce net revenues. The Court then went on to say that there should be enough revenue for operating expenses, for *debt service* and for *stock dividends*. This is quite different from appellant's contention that net earnings should be twice the amount of interest owed. In the instant case, this Commission clearly provided for *operating expenses, depreciation, taxes* and *interest owed*. The 9.35% rate of return provides Appalachian with net operating profits of $46,000,000 annually from the company's West Virginia customers alone. This satisfies the criteria set forth in the *Hope* case.

It is interesting to note that, as Appalachian points out in its Jurisdictional Statement, both *Bluefield* and *Hope* were capitalized mainly by common equity and not debt. The investor interest that the Court alluded to was in fact an investor that had *not* had its company leveraged by its management to 60% plus *debt*. Obviously, the Court in both *Bluefield* and *Hope* could not have intended to equate the investor interest with an amount twice the annual interest requirement on debt *owed:* Especially when the management which leveraged the debt, and the equity investor (Appalachian is wholly owned by American Electric Power Company (AEP)) is for all purposes one and the same.

Appalachian cites *Mississippi Power Company* v. *Mississippi P.S.C.*, 291 So. 2d 541 (1974) as an example of a case wherein an order of a regulatory body was vacated for failure to give adequate consideration to the interest coverage necessary to attract new senior capital.

A close reading of the case indicates that the order was vacated because the Mississippi Commission's decision contained no findings of fact in support of its order, which was against the manifest weight of the undisputed evidence.

In conclusion, Appalachian has not shown confiscation. There is no issue of constitutional confiscation presented to this Honorable Court.

Appalachian's contention that coverage of 2.0 times is a critical test in ratemaking is without merit, and not supported in law, and for the reasons set forth in this section, we respectfully move that the appeal be dismissed, and that the decision of the West Virginia Supreme Court be affirmed.

II. THE WEST VIRGINIA PUBLIC SERVICE COMMISSION DID CONSIDER APPALACHIAN'S CAPITAL ATTRACTION REQUIREMENTS IN ITS ORDERS OF MAY 6, 1977, AND JULY 29, 1977.

The appellant emphasizes on numerous occasions in its "Jurisdictional Statement" that the Commission refused to consider the Capital Attraction Requirements. In fact it devotes a whole main section on pages 14, 15 and 16 of the Jurisdictional Statement entitled "The Commission's Refusal to Consider Capital Attraction Requirements."

These assertions are not consistent with the facts.

The Commission *did consider* Appalachian's capital requirements on pages 22 to 25, inclusive, and page 32 of its order of May 6, 1977, and pages 7 to 9, inclusive of its order of July 29, 1977.

(Appalachian *Appendix*, pages 28-a to 31-a, inclusive, and page 40-a of order of May 6, 1977,

and pages 90-a to 92-a, inclusive of order of July 29, 1977).

(Commission *Appendix*, pages B-28 to B-31, inclusive, B-40 and B-41, and D-9 to D-11, inclusive).

Because of Appalachian's insistence as an integral part of its case that the Commission did not consider these matters, we quote liberally from the Commission May 6, 1977 order (from within the aforesaid cited pages):

> "An equally important consideration in determining rate of return is the necessity for higher earnings. If higher earnings are needed for improvident or excessively accelerated expansion or for excessive return to the common equity owners, the requested rate of return would be too high.
>
> Here, however, Appalachian carried its burden of showing a need for rate of return higher than the 8.73% previously allowed, albeit not at the levels requested. Appalachian presented evidence that its senior securities and commercial paper had been downgraded to be at the lowest rating of all of the major electric utilities in the country. It argues that its debt coverage is dangerously low, so as to limit its ability to finance growth needed for its generating and transmission capacity. Appalachian argues that it needs higher rates to restore to a normal construction level its project 1300 megawatt generating unit partially completed at its site in New Haven, Mason County, West Virginia. In Case No. 8401, by order issued April 29, 1976, this Commission certificated Appalachian's 765-kV high voltage transmission line to run from Culloden in Cabell County to Wyoming County, West Virginia, while recognizing that Appalachian contended that it needed rate relief in Case No. 8182 in order to construct the $72 million project. Appalachian estimates its 1976-1980 construction program will require up to $1.3 billion, which would average $260 million per year. A portion of this financial requirement will be generated internally, with the

> balance raised from investors. In either case, Appalachian will require an improvement in earnings to be able to continue a reasonable growth to satisfy the electricity demands of an energy-short public.
>
> There are several considerations, however, which militate against allowing a rate of return as high as is recommended by Staff or by Appalachian. First, the Commission has been liberal in its allowance of adjustments to fuel expense and other expenses for the second-tier rates. Second, we have permitted a measure of CWIP in rate base. Third, as discussed below, we are allowing a partial normalization of federal income taxes in order to improve the quality of earnings and to encourage growth of plant. Fourth, we have grave reservations about whether or not West Virginia is paying its proper share of total costs vis-a-vis sales by Appalachian subject to other regulatory bodies as discussed below. Finally, the customers of Appalachian in West Virginia are not able to give it *carte blanche* for unlimited rate increases which cannot be absorbed by their limited incomes.
>
> In the light of all of these considerations and the evidence, the Commission finds in its judgment that the allowable rate of return on rate base for Appalachian in this case is 9.35% for West Virginia.
>
> It is hoped that Appalachian will be able to reduce unnecessary or unreasonable costs — such as (1) its cost of coal purchased from its affiliates and (2) other Account 501 fuel costs — in order to earn *more* than 9.35% on total capitalization. The actual results of future fiscal periods will reflect the good or bad results of management decisions, increased sales volumes, and efficiencies that will come with additional modern generating units and high voltage transmission systems. By keeping rates at levels which will recover no more than the lowest possible *reasonable* level of test year costs, we

regulate in a balanced way to induce management to search for cost reductions, prudent growth, and greater efficiencies in operations."

(Commission Appendix, Pages B-29 to B-31, inclusive)

Indeed the Commission did consider the matters, and for valid reasons did not fully agree with Appalachian. It is confusing for Appalachian to now say the Commission did not consider said matters.

We submit that the Commission not only did consider, but fully considered Appalachian's capital attraction requirements.

III. "COVERAGE" REQUIREMENTS IN PUBLIC UTLITY RATEMAKING.

A. WHY THE USE OF A "COVERAGE" REQUIREMENT AS A "CRITICAL TEST" OF CONFISCATORY RATES IN PUBLIC UTILITY RATEMAKING IS UNSOUND, UNRELIABLE, AND JUST PLAIN WRONG.

Bond Coverage is the ratio between net earnings and the Bond Interest owed, i.e. if "net earnings" amount to $4,000,000 and interest expense amounts to $2,000,000, it is said that coverage is 2.0:

$$\frac{\$4,000,000}{\$2,000,000} = 2.0$$

Appalachian has misled this Court by presenting its case in such a manner to show that low revenues are the sole blame for inadequate coverage. The facts are: *That coverage is not dependent solely on revenues, but rather on the numerous factors which make up a public utiity coverage ratio, only one of which is revenues.*

The following data facilitates our review of the development and calculations of net earnings and interest coverage:

TABLE I

Operating Revenues		$580,000,000
Operating Expenses	$380,000,000	
Depreciation	50,000,000	
Taxes Other Than Income	35,000,000	465,000,000
Net Operating Earnings		$115,000,000
Other Income		11,500,000
Net Earnings		$126,000,000
Interest Expense		$ 68,000,000
Coverage		1.85 times

A review of the data in Table 1, above, shows that "net earnings" will vary directly with "revenue" and inversely with "operating expenses," with "depreciation," and with "taxes." An increase of $10,000,000 in revenue will increase net earnings (Table I) and will result in coverage of 2.0, rather than 1.85.

Therefore, following Appalachian's argument, one might be led to believe that the solution to increasing coverage from 1.85 to 2.0 would be to increase revenues by $10,000,000. What Appalachian fails to mention is that: A *decrease* in *expenses*, or a *decrease* in *depreciation*, or a *decrease* in *taxes*, (or a combination), in the amount of $10,000,000 would have the same effect on coverage as increasing revenue by $10,000,000. *Any* action, on the part of the company, which would decrease its deductions (operating expense, depreciation, or taxes) by $10,000,000 would, in the example, increase the coverage from 1.85 to 2.0.

Given the apparent problem facing the hypothetical company in Table I, where does the fault for inadequate coverage lie? Is it in the regulatory commission for not allowing rates sufficient to produce the additional $10,000,000 in revenue, or is it in company management for failing to hold expenditures at lower levels?

A reviewing body must not be misled by Petitioner's narrow argument that additional revenue is the sole solution; and it should be recognized that there are numerous problems, and yes, numerous alternate solutions, in the event of inadequate coverage.

Secondly: The *level* or amount of interest expense, itself, is an essential factor in determining interest coverage ratio. From Table I above we see that coverage is the quotient of earnings divided by interest. As interest expense is reduced, and all other factors remain unchanged, the level of coverage will increase. In the example (Table I), if the interest is reduced by $5,000,000, to $63,000,000, then coverage ratio would increase from 1.85 to 2.0.

From the above it becomes obvious that the *level* or amount of the company's *debt* is a critical factor.

An important point now needs be made. In West Virginia the Public Service Commission, under the law, exercises no control over the capital "leverage" exercised by public utilities. In many states, the public utilities commissions exercise control over the capitalization and capital "leverage" of public utilities.

In our State, the choice and amount of capitalization is a company choice; it is a "management" discretion.

In short, whether a company divides its *Capital:*

10% Debt - 90% Equity, *or*
50% Debt - 50% Equity, *or*
60% Debt - 40% Equity,

is a company or management responsibility. Obviously, a company's total debt interest requirement will vary directly with the amount of total debt.

It also follows that a raise in the *percentage* of *debt* capital, given a fixed Rate of Return, and a fixed interest rate, will *invariably increase* the percentage of the *return on equity*, when the rate of return is more than the interest rate.

Thus, the equity holders do benefit from a percentage increase in debt capital; an increase decided on by management.

Further it follows that where management has a choice of "borrowing" at say 10% or a few days later at 8.5%, a decision to borrow "now" at 10% invariably will enhance the equity return (if we assume the critical test of 2.0). There not only is no incentive to borrow at the lower interest rate, but it becomes "profitable" to the equity holders to borrow at the higher interest rate.

Further, the higher interest amount owed at 10% borrowing, rather than 8.5% borrowing, not only requires a higher revenue level to meet coverage tests (assuming 2.0) but in *itself* becomes a cause of requiring higher revenues because it is a higher expense item.

To demonstrate the effect of management decisions to increase debt capital let us examine the following table:

TABLE 2
Determination of Post-Income Tax Coverage and Return on Equity Assuming a 9% Overall Return and an 8% Interest Rate

Total Capital	$100	$100	$100	$100	$100	$100	$100
Percentage of Debt Capital	10%	20%	30%	40%	50%	60%	70%
Percentage of Equity Capital	90%	80%	70%	60%	50%	40%	30%
Net Earnings from Operations	$9.00	$9.00	$9.00	$9.00	$9.00	$9.00	$9.00
Interest	$ .80	$1.60	$2.40	$3.20	$4.00	$4.80	$5.60
Coverage	11.25	5.63	3.75	2.81	2.25	1.67	1.43
Return on Equity	9.1%	9.25%	9.43%	9.17%	10%	10.5%	11.3%

As is evident from reviewing Table 2 it is desirable, from the stockholder's point of view, for management to utilize capital leverage. As the percentage of equity capital decreases in relation to total capital the equity holders enjoy increased returns on their investment. From the table we see that a company with a very small percentage of debt capital, say 10% debt and 90% equity, if allowed to earn an overall return on 9%, will earn 9.1% on equity. This same company will have an interest coverage of *11.25 times*. As the company increases its percentage of debt capital, say to 20% debt and 80% equity, the return to equity holders increases to 9.25%. The off-set, however, is that coverage drops to *5.63 times*. As a company increases its percentage of debt to a very highly leveraged level of 60% the return on equity raises to 10.5%. The problem with extensive debt levels, however, is evident in the fact that at 60% debt and 40% equity the coverage has dropped to *1.67 times*.

Over the past five calendar years Appalachian's senior capital as a percentage of total capital has ranged from 67.51% to 70.23%.

TABLE 3
APPALACHIAN CAPITAL STRUCTURE

Particulars	1976 (000)	1975 (000)	1974 (000)	1973 (000)	1972 (000)	Average of 5 yrs.
Long-Term Debt:	60.58	60.72	56.35	58.08	60.87	59.32
Short-Term Debt:	.67	.07	5.51	1.57	.49	1.66
Preferred Stock:	7.28	7.82	8.41	7.86	8.88	8.05
Total Senior Capital:	68.53	68.61	70.27	67.51	70.23	69.03
Common Equity:	31.47	31.39	29.73	32.49	29.77	30.97

Note: 1976 Figures are estimates
Source: Company Annual Reports

The result of a high debt ratio is a tendency for interest coverage to decline. A company can provide its stockholders with maximized returns through employment of capital leverage. Why then, when management decisions begin to show weaknesses of declining interest coverage, should the company look to the ratepayers to offset the declining coverage levels through higher rates?

For the purpose of analyzing effects of management decisions on coverage and equity return the following table will be helpful:

TABLE 4

Debt	$ 60 at 8%	=	$4.80
Equity	$ 40	=	4.80
Total	$100	=	$9.60

In this example, a company has total capital of $100, consisting of $60 debt and $40 equity. With the debt rate equal to 8%, the cost of debt is $4.80. Therefore, to maintain an aftertax coverage of *two times* it is necessary for the equity to earn $4.80 for a total after tax earnings of $9.60.

Let us assume that this hypothetical company, a regulated utility, has been assured that it will be allowed to maintain the two times coverage. Let us further assume that the company is faced with retiring its $60 debt and management has been counseled that an immediate debt issue will be at a 10% rate. On the other hand, there are strong indications that capital pressure is about to decline and interest rates will ease so that an offering in 45 to 60 days may be marketed at 8.5%. Given this set of circumstances, what choice should be made by management?

The following table shows the results (given the two times coverage guarantee) of the two alternatives:

TABLE 5

	1 - Borrow at 10%		2 - Borrow at 8.5%	
Debt	$ 60 at 10%	$ 6.00	$ 60 at 8.5%	$ 5.10
Equity	$ 40	$ 6.00	$ 40	$5.10
Total	$100	$12.00	$100	$10.20

The reward to equity holders of an imprudent management decision is evident. In the original table, (with an 8% interest rate) the earning on equity required to maintain the two times coverage was $4.80. Therefore, equity holders were earning at a rate of 12% ($4.80 divided by $40). Under alternative one, borrowing now at 10%, the return to equity holders will jump to 15% ($6 divided by $40) if the two times coverage is to be maintained. On the other hand, if management elects to follow prudent judgment and borrow at 8.5% the return to equity holders is only $5.10, or *12.75%*, if the two times coverage is to be maintained.

We see now that the result of "covering" each additional interest dollar at least *twice* is a *bonanza* for

the company's common equity holders. We submit that this concept of "cost-plus" and its resulting management inefficiency is what Appalachian Power Company is requesting.

Using our simplified example, what if the company required additional financing of $15 even at the original 8% interest rate? If the company elected to finance the entire $15 through debt the result would appear as follows:

TABLE 6

Debt	$ 75 at 8%	=	$ 6.00
Equity	$ 40	=	$ 6.00
Total	$115	=	$12.00

Because of the additional interest requirement, even at the same 8% rate, in order to maintain a two times coverage the equity earnings must increase to $6, and the resulting return to equity holders would be *15%* ($6 divided by $40). Hence, we again see the enhancement of equity return through utilization of capital leverage. Merely by deciding to finance the $15 totally through debt the company has provided for a return on equity of *15%* in place of 12%.

Operating with the constraints of the two times requirement what decision will this company make if told that the additional $15 in debt will result in closer market scrutiny of the company's excessive debt ratios and an increase in its interest rates from 8% to at least 9%? Once again, maintaining a two times coverage, such an increase would enhance and further increase the return to the equity holder. The $75 debt at a 90% rate of interest would require $6.75. The equity earnings requirement then would increase to *$6.75* in order to maintain the two times

coverage and the resultant return to common equity holders would be *17%* ($6.75 divided by $40).

Interest charges on Appalachian's long-term debt has risen from $36,160,000 in 1972 to $71,455,000 in 1976. Appalachian has obviously chosen to increase debt at a time when interest rates are highest.

TABLE 7
APPALACHIAN INTEREST COST
AS OF DECEMBER 31

Particulars	1976 (000)	1975 (000)	1974 (000)	1973 (000)	1972 (000)
1. Interest Charges on Long-Term Debt:	71,455	64,954	48,743	43,398	36,160
2. Interest on Short-Term Debt:	800	76	8,719	1,485	236
3. Average rate % of Long-Term Debt:	7.86	7.64	6.63	6.55	5.85
4. Average % Rate on Short-Term Debt:	8.00	7.63	12.12	8.30	4.72
5. Weighted Average Cost of Long-Term Debt: %	4.76	4.64	3.74	3.80	3.56
6. Weighted Average Cost of Short-Term Debt: %	.05	.01	.67	.13	.02
7. Total Weighted Cost:%	4.81	4.65	4.41	3.93	3.58

This Commission cannot condone, and our earnest hope is that this court will not condone, regulatory policies which could conceivably reward poor or imprudent management through enhancement of equity returns.

To establish as a critical test the 2.0 coverage requirement, will open the door of the public utility regulation field to higher and higher profits, as well as higher and higher customer rates to support the capital structure "body", the head of which is interest "coverage", and the tail of which tags along, which is the equity return.

It should be kept in mind that what Appalachian complains of, asserting a 1.80 coverage which inevitably will be greater, is *not* that it is losing money; but that its *Return* or Net Earnings should be higher. In fact the Commission in Case No. 8182 provided for almost $46,000,000 as an annual amount of return.

For these reasons, we submit that it is unsound, unwise, and wrong to adopt the 2.0 coverage test as a critical test of confiscation.

The problem is further compounded when a public utility makes customer sales in more than one state, and also makes sales governed by the Federal Power Commission. Appalachian was granted a twenty-five percent (25%) increase in its sales for resale rate before the FPC in July of 1977. Appalachian was also granted increased rates by the Virginia Commission effective November 1, 1977. Are West Virginia subscribers required to subsidize Virginia ratepayers when Appalachian's earnings are deficient there? They will if the coverage test is used to determine confiscation. Assume that in all of its operational jurisdictions, plus FPC, the utility shows a negative coverage test. How then should the responsibility for meeting the 2.0 test be managed? Which jurisdiction? How much? How do we synchronize this support of the utility?

Here the intrastate aspect of sales to customers becomes not only a term of description, but a reality, and in the real world of service to West Virginia customers, the Commission rightly reviews the evidence *only* relating to the West Virginia operation. What is a reasonable, just, and fair, rate for the West Virginia customers? That is the principle which guides the West Virginia Commission; not a "critical test" that may first appear in the company indenture, and becomes a "Statement of Policy" of the Securities and Exchange Commission.

Of lesser consequence, is the choice that company management has of what part of its income to pay out as dividends, and what part to retain as earned surplus.

A company may easily have, for five to ten years, a "dividends" profile of exceedingly high declarations. This results in equity being lowered and debt being increased, with accompanying increases in total interest. Now that it "needs" money to cover its "interest" is it right to expect that "dividends" continue at a high level while the required interest *coverage* dollars, in excess of actual interest requirements, are obtained from ratepayers?

All of these considerations lead to the conclusion that the interest "coverage" requirement of 2.0 is unsound, and we earnestly submit to this Court that such a "critical test" should not become a part of sound public utility rate making.

B. COMMENTS ON EXACTLY HOW 2.0 TIMES COVERAGE AFFECTS EQUITY LEVELS

Appalachian in its Jurisdictional Statement raises two questions or issues. The first is: Must a State Public Utility Regulation Commission, as a matter of law, establish rates, whether otherwise justifiable or not as reasonable and just, which rates would return to the utility as *net earnings* twice the amount of the interest owed by the public utility, irrespective of the amount of the debt, the rate of interest, or of the numerous management decisions involved, which decisions result in not only the overall level of debt capital, but also which decisions affect other factors which result in defined net earnings.

Appalachian is contending that a test of the reasonableness of rates granted by a state regulatory agency must be predicated on those rates producing net earnings before

interest which are equal to at least two times the annual interest requirement of the public utility. Under such a test, a utility could be given exorbitant, unwarranted, and unconscionable profits for its equity by employing unwise and unsound management decisions with regard to debt levels.

In brief, as a matter of law, does the United States Consitution, Fifth and Fourteenth Amendments, guarantee to a utility such as Appalachian that its net earnings before interest expense must be at least $40,000,000 when its annual interest on long-term debt is $20,000,000; that if its interest becomes $35,000,000 (for whatever reasons) the net earnings must equal or exceed $70,000,000; and when the interest expense grows to $70,000,000 the net earnings must equal or exceed $140,000,000? Appalachian is maintaining that such a progression of net earnings is "guaranteed" as follows:

Annual Interest	Net Earnings Before Interest	Net Earnings for Stockholders
$20,000,000	$ 40,000,000	$20,000,000
35,000,000	70,000,000	35,000,000
70,000,000	140,000,000	70,000,000

As can be seen, Appalachian's issue regarding coverage is based on a guaranteed dollar for dollar increase in earnings available for stockholders as its interest expense is increased, regardless of the justification for such an increase in earnings to stockholders and regardless of the rate of return on stockholder's investment which may result.

In a simple situation, under Appalachian's insistence that earnings must be maintained at two times the level of interest on long-term debt, if the *interest expense* of a company grows from $35,000,000 to $70,000,000, then the portion of net earnings available to equity holders must grow to provide two dollars of the pre-tax earnings for each dollar of interest expense. Appalachian holds that it is constitutionally guaranteed that rate payers pay rates sufficient to provide such an increase in earnings to stockholders regardless of the level of capital invested by stockholders.

Let us assume that when debt cost was $35,000,000 the regulatory commission allowed earnings, before interest, of $91,000,000, leaving a balance of $56,000,000 for stockholders. If stockholder investment amounted to $300,000,000 in this business the resulting return on stockholders' equity would be 18.7%, a very substantial figure. Furthermore, since the coverage of interest is 2.6 times (91 ÷ 35) no one could say, on the basis of any conceivable "test" that the rates contributing to a 2.6 times interest coverage level and a 18.7% return on equity could be unconstitutional. Let us further assume, however, that in a subsequent year, because of increasing interest levels and rates, the company's annual interest increases to $70,000,000. The regulatory agency determines that the additional $35,000,000 expense should be recovered through rates and, consequently, approved rates which result in an increase in net earnings before interest of $35,000,000, up to the level of $126,000,000 ($91,000,000 plus $35,000,000). The balance, available to stockholders, remains at $56,000,000 and the rate of return on stockholder's investment remains at 18.7%. However, the coverage of interest is now reduced to 1.8 times (126 ÷ 70). Appalachian argues that *now* the $56,000,000 profit on equity is *unconstitutional* because the net defined earnings are not sufficient to "cover" interest two times.

Under Appalachian's approach of constitutional tests for reasonableness of a utility's earnings, $56,000,000 profits on equity resulting in a 18.7% return on stockholder's investment is constitutional if the company's annual interest on debt is $35,000,000; but $56,000,000 profits on equity resulting, in a return on stockholder's investment of 18.7%, is unconstitutional when annual interest on debt becomes $70,000,000.

Under Appalachian's approach, the earnings on equity, in the above cited example, *must* increase from $56,000,000 to a *minimum* of $70,000,000 (increasing return on investment to 23%) merely because of the increased expense. The equity earnings in this case accrue to the sole stockholder: The American Electric Power System (hereinafter "AEP").

IV. AS A MATTER OF FACT, WHAT IS APPALACHAIN'S FIRST MORTGAGE BOND "COVERAGE" IN 1977?

The following data is based on Company Annual Reports and Financial Statements.

Appalachian's total company coverage for calendar year ended December 31, 1976, for first mortgage bonds was *2.0* times.

Indeed, Appalachian issued First Mortgage Bonds three times in *1975* in the amount of $150,000,000 and twice in *1976* in the amount of $130,000,000.

The appellant, Appalachian, poses its argument as if the only way to improve coverage is to receive additional revenues from its customers. One significant way to improve coverage that the company conveniently overlooks, is a reasonable modification of its capital structure.

On December 31, 1976, Appalachian's capitalization consisted of 32% common stock, 7% preferred equity, and *61%* long-term debt. This Commission is no way responsible for Appalachian placing itself in such a highly leveraged position with the expensive levels of long-term debt.

Likewise, the return on common equity, based on 1976 cost levels of long-term debt and preferred stock, and based on an overall rate of return of 9.35% (granted by this Commission in Case No. 8182) amounts to *13.2%* for Appalachian.

Now, a reasonable modification of capital structure, in view of coverage difficulties, to a 55% long-term debt (from 61%), to 38% common equity and 7% preferred equity, would improve the company's coverage position for the year ended December 31, 1976, from 2.0 to *2.3*. But, the common equity return would reduce from 13.2% to 12.3%, which surely is still well within the zone of reasonableness. The company, exercising management discretion, chose to *not* modify its capital structure. We now make an important point. In West Virginia, this Commission does not rule on or control a public utility's capitalization. The public utility has full control of its capitalization ratios.

Clearly, we are indicating that factors other than revenues substantially affect the amount of coverage.

The company's coverage as of August 31, 1977, for first mortgage bonds, at Commission granted "tier two" rate levels is 1.85 times. An increase of $9.6 Million in revenues would indeed bring this twelve month period coverage level up to 2.0 times.

This Commission, in its Case No. 8182 (reopened), did grant Appalachian additional rates effective May 1, 1977, which have the effect of increasing revenues $10,000,000 annually. (Appendix beginning at Page F-1). Additionally, the Virginia Corporation Commission has granted Appalachian increased rates effective November 1, 1977; and the Federal Power Commission granted increased rates effective July 1, 1977. (Incidentally the rates granted by the Virginia Corporation Commission, effective November 1, 1977, produce a Rate of Return of 9.14%, being less than the West Virginia Rate of Return for Appalachian of *9.35%*).

More importantly, respecting West Virginia, Appalachian has completely failed to disclose two items which materially affect its coverage for the twelve-month period ended August 31, 1977.

The first is a depreciation expense item of $1.4 Million which inflates expenses. Appalachian hereby employs an improper accounting method and one not approved by this Commission. For coverage calculation purposes, Appalachian added this $1.4 Million as an expense. It seems that the company is just determined to paint the worst picture, improperly, and then to blame this Commission for its "low" coverage levels.

The second item which Appalachian has conveniently failed to disclose relates to approximately $90 Million invested in subsidiary companies (primarily coal mining). This investment of Appalachian is funded by its total capital, which is 61% debt. A substantial portion of Appalachian's interest expense is associated with these investments in the subsidiary companies. Yet, Appalachian fails to file a consolidated income statement and thereby fails to include $5,000,000 in earnings of its subsidiaries in its coverage calculations. This failure in

no way is due to any directive or order of this Commission, but is a management decision of Appalachian.

A meaningful effort by the company to reflect its coverage accurately for the year ended August 31, 1977, should certainly include the $1.4 Million and the $5 Million which alone would improve August coverage for first mortgage bonds from 1.85 times to 1.95 times; and when we reflect the four months of granted West Virginia tier-three rates from May 1, 1977, through August 31, 1977 ($3.3 Million), the first mortgage bond coverage then exceeds *2.0 times*, as of August 31, 1977.

These are the vagaries of management decision that make unreliable the coverage requirement of 2.0 times as a critical test or as a "must" in public utility ratemaking.

United Fuel Gas Company v. *Railroad Commission*, 278 U.S. 300 49 S.Ct. 150, 73 L.Ed. 390, (1929) holds: A public service corporation cannot make a rate confiscatory by reducing its net earnings through the device of contract unduly favoring a subsidiary or a corporation owned by its stockholders.

And, likewise, Appalachian should not reduce its net defined earnings by failure to include subsidiary earnings.

V. SOME COMMENTS ON APPALACHIAN'S CREDIT STANDING

In its Jurisdictional Statement, Appalachian, on Page 17, refers to downgrading by Standard and Poor's of its First Mortgage Bonds. It relates this downgrading to an "impairment of credit", and then lays the "erosion" of the credit at the doorstep of the Commission.

However, a close reading of Standard and Poor's statement on Page 17, Jurisdictional Statement, demon-

strates that the "changed rating" of First Mortgage Bonds is based on three reasons.

One is *the high percentage of long-term debt in its (Appalachian's) capitalization.* We have dealt at some length in the previous section and other sections on the effects of an unusually high percentage of long-term debt. Such a high percentage is damaging in numerous ways.

Indeed, Appalachian's own witness, H. Russell Fraser, in Case No. 8182, Page 1890, Transcript, deems the management decision to forego a "less conservative capitalization" as being an important factor in the position Apppalchian finds itself in.

Second is *the sizeable amount of revenues being collected subject to refund.* While indirectly this Commission may be said to be a cause of this, more directly, the company practice of filing for *twice* or more the amount of rate increase later found to be reasonable and just, causes the high amount of revenues collected subject to refund.

Third is the *less than adequate rate relief granted the company over the past several years,* particularly in West Virginia . The words used do include Virginia and the Federal Power Commission. And, any inadequate rate relief in large measure may have its genesis in an extremely high percentage of long-term debt, and its cure in a more reasonable percentage of long-term debt.

We do not dispute the company's evaluation of its credit position but we find it extremely difficult to believe with the company, that it arrived there free of the blemishes and bruises that came as a result of "management decisions". Again, we stress that in West Virginia, (contrary to the position on Page 15 of the Jurisdictional Statement re: this Commission's responsibility as to regulating the reasonableness of Appalachian's capital struc-

ture) this Commission does not, and has never, regulated capital structure. Such is a company responsibility, and thus the company must live with the fruit that its decisions bear.

VI. THE COMMISSION ORDERS DO NOT UNCONSTITUTIONALLY BURDEN OR INTERFERE WITH INTERSTATE COMMERCE.

The Appellee submits to this Honorable Court that the West Virginia Public Service Commission orders in Case No. 8182 do not unconstitutionally burden or interfere with interstate commerce. Moreover, the Appellant in presenting this second question has based its issue on the fact that the rates ordered by the Commission in Case No. 8182 are so low as to preclude the Appellant from raising capital necessary for timely construction of facilities and therefore burden interstate commerce. As hereinbefore discussed, it is submitted that the Appellant has failed to demonstrate that its rates are legally confiscatory as to preclude it from raising the necessary capital to *timely* construct facilities for its customers. For that reason, the Appellee contends that the rates imposed by this Commission in no way burden interstate commerce.

The Appellant contends that Appalachian is engaged in interstate commerce as it transmits energy across state lines. The Appellee readily agrees that this statement is true; however, it is submitted that the case at bar concerns the sale of electricity of an *intrastate* nature over which the Appellee has, by law, jurisdiction. The Federal Power Act (16 U.S.C. §824), explicitly grants the Federal government jurisdiction only to those matters which are not subject to regulation by the states. Section 201(a), Part II of the Federal Power Act states the following:

> "It is hereby declared that the business of transmitting and selling electric energy for ultimate distribution to the public is affected with the public interest, and the federal regulation of matters relating to generation to the extent provided in this Part and the Part next following and of that part of such business which consists of transmission of electric energy and interstate commerce and the sale of such energy at wholesale interstate commerce is necessary in the public interest, such federal regulation, however, *to extend only to those matters which are not subject to regulation by the states* . . . (emphasis provided)

The matters before the West Virginia Public Service Commission concern only sales of electricity of an *intrastate* nature, and not sales at *wholesale.* It is submitted by the Appellee that the matters that are before this Honorable Court concern local rates and therefore do not per se constitute interference with interstate commerce. In the case of *Preston County Light and Power Company* v. *Public Service Commission of West Virginia,* 297 F.Supp. 759, 763 (S.D. W.Va. 1969), the District Court held as follows:

> ". . . Mere inadequacy of a local rate prescribed by competent authority does not per se constitute interference with interstate commerce. There is, however, apparently, no established rule as to what degree of affect on interstate commerce is sufficient to constitute an interference therewith. To say that the degree of interference must meet the limit of confiscation of property begs a question, since there are no well defined guidelines of the degree of effect that amounts to confiscation. Each case must necessarily be dealt with on its own facts and circumstances. Assuredly, if the rates involved in the present case were found to directly interfere with interstate commerce by being confiscatory or otherwise, the Johnson Act would, of course, not be applicable . . ."

The rates that are in question in the case at bar are of a local nature and do not involve interstate commerce and further, these rates are not confiscatory within the guidelines established by the United States Supreme Court as hereinbefore discussed. In the case of *Kansas-Nebraska Natural Gas Company* v. *The City of St. Edward*, 134 F. Supp. 809, 825 (D. Neb. 1955), the District Court stated the following:

> ". . . The Congress thus left to the state the problem of regulating the local distribution and marketing and sale price of natural gas, notwithstanding its importation for that purpose in interstate commerce . . . Mere inadequacy of a local rate prescribed by a competent authority for natural gas imported by interstate pipeline 'interfer[s] with interstate commerce' . . . That the rate prescriptions of several ordinances, indirectly and incidently affect interstate commerce may be granted; it does not follow therefrom that they interfere with such commerce . . ."

The Appellee contends that the rate prescriptions of this Commission's orders have at the most only an indirect and incidental effect upon interstate commerce.

In the case of *Zucker* v. *Bell Telephone Company of Pennsylvania*, 373 F.Supp. 748, 751 (E.D. PA. 1974); aff'd. 510 F2d 971 (1975); cert. denied, 422 U.S. 1027 (1975), the Eastern District Court of Pennsylvania held as follows:

> ". . . The courts have found that state agency orders applicable to intrastate telephone rates do not interfere with interstate commerce . . ."

Upon analyzing and perusing the Appellant's jurisdictional statement one would be led to believe that if this Honorable Court does not grant the relief that the Appellant is seeking, the entire country would be estopped from conducting its normal business for the reason that

Appalachian will not be able to provide electricity. Obviously, this argument or contention is without merit in that Appalachian is only one of a host of electric generating companies in the nation that are providing electricity for energy needs. In addition, there are multitudes of other energy resources which our nation is relying upon for energy needs. The appellant has created an obvious hyperbole that does not exist.

The Appellant discusses the scope of its responsibility in providing service and contends that this service reaches beyond the State of West Virginia to retail customers in Virginia and to twenty-one firm wholesale customers in Virginia, West Virginia and Tennessee. It further states that it supplies wholesale electric service (non-firm) both within and outside of its retail market area directly and indirectly by bulk transmission or displacement not only to the integrated American Electric Power System but also to 26 major utilities supply systems that makeup the regional grid known as the East Central Area Reliability Group (ECAR) and through system interconnect, non-ECAR electric utilities which include TVA, Carolina Power and Light, Duke Power, Commonwealth Edison, Illinois Power, Central Illinois Public Service Company; however, the Appellant has failed to disclose further factors which are important regarding this issue.

The Appellant's own witness, Mr. Theodore J. Nagel, Senior Executive Vice-President and Assistant to the Chairman of American Electric Power Service Corporation stated concerning "non-firm" sales during the course of proceedings before the Commission that "neither APCo or AEP plans or constructs facilities for short-term, limited term or unit power sales." (See Appalachian Power Testimony of T. J. Nagel, West Virginia P.S.C. Case No. 8182, Applicant's Exhibit "U"). Mr. Nagel has testified that the construction project which is an issue in the case

at bar is not being constructed to serve the ECAR group and interconnected non-ECAR electric utilities such as TVA, Carolina Power and Light, Duke Power, Commonwealth Edison, Illinois Power, Central Illinois Public Service Company.

The entire cost of Appalachian's construction program will be borne by West Virginia and Virginia retail customers and firm wholesale customers. Other than those customers, none of the other entities mentioned by the Appellant will contribute fairly to the cost of the construction program during the construction period. Only after the construction is completed and those "non-firm" customers are receiving additional power will said other customers begin providing compensatory revenues to Appalachian Power Company in recognition of the cost of newly constructed facilities.

Further, it is submitted that the Appellant's method of financing this construction project may not be the most efficient. For example, in another parent Power System, various member utilities will share on a pro rata basis the cost of construction and ownership of a plant which will provide electricity to many jurisdictions and thus reduce the financing burden in a given jurisdiction. The American Electric Power System has chosen another method of alternative construction of large increments of capacity by member utilities. During the construction period the member responsible for such construction is faced with supporting the capital costs during an interim period without a sharing of such costs with other members of the system. The West Virginia Public Service Commission's sole concern by law is with the protection of the West Virginia retail customers and the West Virginia utilities. This Commission seeks in the orders of this case as well as others to render equitable and just rate orders that will be fair to the consumers of this State of West

Virginia as well as to utilities such as the applicant engaged in providing electric service in West Virginia.

Moreover, as has been previously discussed, the Appellant obviously has not done all it could to improve its financial situation. For example, Appalachian Power Company has invested approximately $90,000,000 in subsidiary companies principally involved in coal mine operations. Would not Appalachian's needs for external financing of production facilities be reduced through its own initiative by selling a portion or portions of this coal property? If a choice must be made between needed capacity for generating electricty and investments in coal reserves, the time may have come for Appalachian to reassess its part in such and leave coal mining to coal mining companies.

The Appellant further contends that the Commission orders impose a burden on and interfere with interstate commerce by prescribing rates so low so that timely completion of the Company's construction of its portion of the planned AEP systemwide construction program is imperiled. The Appellee contends that the Appellant is premature in its contention. The completion date of the construction project is 1981 and needed financing is required in 1978, 1979, 1980, and 1981. The rate orders in the case at bar are applicable to a period substantially prior to those dates. The Commission cannot be required to render rate orders which will infinitely solve or remedy all problems. There are too many variables which will affect rates between now and 1981. Moreover, in addition to Appalachian doing what it can through prudent management decisions to improve its financial status, the Appellant also has the opportunity to seek new rates through new rate cases. The case of the *Federal Power Commission* v. *Hope Natural Gas*, 320 U.S. 591, 615 (1944), is cited for that proposition. The United States

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Supreme Court, as quoted heretofore in this Brief, held as follows:

> "... It is suggested that the Commission has failed to perform its duty under the Act in that it has not allowed a return for gas production that will be enough to induce private enterprises to perform completely and efficiently its functions for the public. The Commission, however, was not oblivious of those matters. It considered them ... No serious attempt has been made here to show that they are inadequate. We certainly cannot say that they are, unless we are to substitute our opinions for the expert judgment of the administrators to whom Congress entrusted this decision. Moreover, if in light of experience they turn out to be inadequate for development of new sources of supply, the doors of the Commission are open for increased allowances. This is not an order for all time. The Act contains machinery for any adjustments..."

It is again pointed out to this Honorable Court that the Appellant has pending with this Commission a *new* rate filing, Case No. 9091, filed September 12, 1977.

Appellant has further alleged that the Commission orders impose an impermissible burden on and interference with interstate commerce by prescribing rates so low that timely completion of the Company's construction of its portion of the planned AEP systemwide construction program is imperiled. The Appellant then cites the case of *Southern Pacific Company* v. *Arizona*, 325 U.S. 761 (1944) for the proposition that the Commission has overstepped the bounds of reasonableness and that the Court as a final arbiter must engage in appraisal and accommodation of the competing demands of the state and national interests involved. The Appellant goes on to state that the Commission's orders impose a serious burden on interstate commerce conducted by the Appel-

ant and proposes a substantial obstruction to the national policy proclaimed by Congress of assuring an abundant supply of electric energy to the United States with the greatest possible economy and with regard to the proper utilization and conservation of natural resources.

The Appellant is attempting to raise a "national interest issue" which does not exist. It is submitted that the *Southern* case can be distinguished from the case at bar on the basis that the national commerce that the Appellant is alluding to in its jurisdictional statement is futuristic. There is nothing in the record to indicate that the Appellant's ability to transmit electricity on an interstate basis will at all be affected in the year 1978 nor any of the prior periods of 1975 and 1976 that Case No. 8182 concerns. To raise the national interest issue at this point in the proceeding is totally without merit.

The national commerce spoken of in the *Southern* case is one that is real and demonstrative. The commerce that Appalachian alleges will be affected by the Commission's rate orders is futuristic and speculative at best. On page 767 of *325 U.S.* (the *Southern* case), the court stated as follows:

> "... When the regulation of matters of local concern is local in character and effect, and its impact on the national commerce does not seriously interfere with its operation, and the consequent incentive to deal with them nationally is slight, such regulation has been generally held to be within state authority..."

The Court stated further on page 770 of *325 U.S.* the following:

> "... There has thus been left to the states wide scope for the regulation of matters of local state concern, even though it in some measure affects the

commerce, provided it does not merely materially restrict the free flow of commerce across the state lines, or interfere with it in matters with respect to which uniformity of regulation is of predominant national concern . . ."

In conclusion, it is submitted that the commerce in this case at bar is one of a local nature and affects intrastate commerce only. There is absolutely nothing in the record of these proceedings to demonstrate that the flow of interstate commerce will in any way be impeded. Further, the Appellant's attempt to raise the national commerce issue is futuristic and has no application to Case No. 8182.

It is therefore concluded and respectfully submitted that the Commission orders in question do *not* unconstitutionally burden or interfere with interstate commerce.

ARGUMENT — SUMMARY

The Commission orders in question establish rates for Appalachian for the period from August 28, 1975 through April 30, 1977.

Appalachian while contending ex post facto confiscation did issue first mortgage bonds three times in *1975* and twice in *1976*. Its coverage on December 31, 1976 exceeded 2.0 times.

Appalachian plans to again issue First Mortgage Bonds in late 1978. Its increased rates by the West Virginia Commission effective May 1, 1977; by the Federal Power Commission effective July 1, 1977; and by the Virginia Corporation Commission effective November 1, 1977; should establish its coverage ratio well in excess of any indenture "requirement" of 2.0 times.

Especially when, as demonstrated above, exclusion of non-approved accelerated depreciation expense ($1.4

Million), and inclusion of subsidiary earnings ($5 Million) is effected, the Company's coverage exceeds 2.0 times even as of August 31, 1977.

More importantly, the imposition of *new* rates in West Virginia, effective March 1978, in the amount of at least $47,000,000 over and above approved West Virginia rates would, according to the company, permit it to issue the First Mortgage Bonds in late 1978. (This is subject to future Commission consideration).

As of a given time, there has never been an issue.

There is *no* unlawful confiscation which has deprived Appalachian of property without just compensation. The rates established are well within the zone of reasonableness. There is no violation of the requirements of the Fifth and Fourteenth Amendments of the United States Constitution.

Additionally, there is no violation of Article I, Section 8, Clause 3 of the United States Constitution, relating to the power of Congress to regulate commerce among the states.

First: There is *no* commerce regulated by Congress to be interfered with. *Second:* Local public utility ratemaking is not *per se* interference with interstate commerce. *Third:* The *confiscation* that Appalachian says "interferes" does not exist. *Fourth:* The "commerce" that Appalachian fears will be interfered with is futuristic (1981 and beyond) and vague and specious, just as is the issue raised with respect to interference with interstate commerce.

In closing, the company raises the problem of the "energy crisis" and in so doing adroitly island-hops over the constitutional issues, which do not readily bend to a decision for the company, to the national policy of the

Chief Executive and of Congress, and quotes the President from the New York Times regarding "the moral equivalent of war".

While the President has identified and characterized the energy crisis as the moral equivalent of war, such characterization certainly was not meant to give the electric utility industry a license to use, without recompense, the monies of the consuming public gathered now to build its plants in the future.

As stated above, the net effect of this appeal so far has been to delay the October 1977 refund, a refund of rates paid by West Virginia ratepayers in excess of rates found to be reasonable and just by the only administrative body which, by law, may establish rates in West Virginia. These refunds belong to the ratepayers. If any confiscation has occurred, it is by the company of the ratepayers' monies.

For the foregoing reasons, it is respectfully moved that the appeal be dismissed.

CONCLUSION

For all of the foregoing reasons the appellee, Public Service Commission of West Virginia, respectfully moves that the appeal herein be dismissed and that the order of the West Virginia Supreme Court of Appeals of October 10, 1977, affirming Commission orders of May 6, 1977, and July 29, 1977, in Commission Case No. 8182, upon the matter of Increased Rates and Charges of Appalachian Power Company in West Virginia, be affirmed; and that said Motion be granted on the grounds that no substantial federal questions have been presented.

Respectfully submitted,

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Public Service Commission of West Virginia
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February 8, 1977

Supreme Court, U. S.
FILED
FEB 8 1978
MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

October Term, 1977

No. 77-979

Appalachian Power Company,
Appellant,

v.

The Public Service Commission of West Virginia,
Appellee.

ON APPEAL FROM THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

APPENDIX TO MOTION TO DISMISS OR AFFIRM AND TO BRIEF IN SUPPORT THEREOF

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STATE OF WEST VIRGINIA

At a Regular Term of the Supreme Court of Appeals continued and held at Charleston, Kanawha County, on the 10th day of October, 1977, the following order was made and entered, to-wit:

APPALACHIAN POWER COMPANY, a corporation
vs.
THE PUBLIC SERVICE COMMISSION OF WEST VIRGINIA

Upon an appeal from, suspension and review of the final order of the Public Service Commission of West Virginia made and entered on May 6, 1977, as revised, modified and affirmed by the Commission's Order issued on July 29, 1977.

The Court, having maturely considered the petition; amended petition; note of argument in support thereof; the record consisting of all papers, documents and evidence which were before the Public Service Commission at the hearing which resulted in the entry of the final order complained of; the statement of reasons for the entry of its order of the 6th day of May, 1977, as revised, modified and affirmed by the Commission's Order issued on July 29, 1977, filed herein by the respondent, Public Service Commission of West Virginia on October 3, 1977; and the oral argument of counsel on the 4th day of October, 1977, the date fixed by the Court for hearing upon the aforesaid petitions; is of opinion that the petitioner has not shown itself entitled to the relief prayed for in its said petition. It is therefore considered and ordered that the prayer of the petition for an appeal from, suspension and review, in this proceeding, be, and the same is hereby, denied. Justice Miller would grant.

It is further ordered that leave be, and the same is hereby, granted to the Public Service Commission of West

Virginia to withdraw from the office of the Clerk of this Court, the record consisting of all papers, documents and evidence originally filed with the Public Service Commission of West Virginia.

A True Copy

Attest:

s/ GEORGE W. SINGLETON
Clerk Supreme Court of Appeals

PUBLIC SERVICE COMMISSION
OF WEST VIRGINIA
CHARLESTON

At a session of the PUBLIC SERVICE COMMISSION OF WEST VIRGINIA at the Capitol in the City of Charleston on the 6th day of May, 1977.

CASE No. 8182

APPALACHIAN POWER COMPANY, a corporation.

In the matter of increased
rates and charges.

PROCEDURE

On March 31, 1975, Appalachian Power Company, a corporation (hereinafter "Appalachian" or "company"), filed its tariff designated P.S.C. W. Va. No. 3, cancelling P.S.C. W. Va. No. 2, stating increased rates and charges and certain modified rate designs for furnishing electric service in the entire territory served by it in the State of West Virginia, to become effective May 1, 1975. This filing included accounting data required by our Tariff Rule 42 based on a calendar 1974 test year.

By order entered on April 4, 1975, Appalachian was made respondent to this proceeding and pending investigation, hearing and decision said revised tariff was suspended and the use of the rates and charges stated therein deferred until August 28, 1975. It was further ordered that if the case had not been finally decided at the expiration of the aforesaid suspension period, such rates and charges applied for could not be placed into effect until a bond in the amount of Thirty Million Six Hundred Thousand Dollars ($30,600,000) with interest thereon, be given and approved by the Commission.

By order entered on June 3, 1975, the matters involved herein were set for hearing in the Commission's Hearing Room at the Capitol in the City of Charleston on July 21, 1975, at 9:30 a.m., EDT, and the company was required to give proper notice to the public.

By order entered on August 18, 1975, the Commission set the interest rate on refunds secured by the bond at 7¾%.

Proper notice was given and hearings were held on the following dates: July 21, 27, and 30, 1975 (consolidated with Appalachian Cases Nos. 7083—Reopened, 8192 and 8235); August 5, 1975; January 12 and 13, April 21, 22 and 23; June 7; July 12 and 13; August 10, 11, 12 and 31, 1976.

At the various hearings herein the company was represented by Charles R. McElwee and Samuel M. Sugden, attorneys at law, and the company's testimony was adduced from sixteen witnesses. The staff was represented by E. Dandridge McDonald, attorney at law, Legal Division; George R. Heath, Laxmi N. Mehra, David Ellis, and Robert Stier, Division of Accounts, Finance and Rates; and C. William Wensyel, Division of Engineering. Three witnesses were presented by staff. Attorneys for various intervenors were: Robert R. Rodecker, representing Appalachian Research & Defense Fund, Inc., Mercer County Economic Opportunity Corporation, and McDowell County Consumer Action Council, Inc.; Vincent V. Chaney and Michael T. Chaney, representing the City of Charleston and the City of South Charleston; T. D. Kauffelt, representing FMC Corporation; and John C. Lobert and C. E. Goodwin, representing ACF Industries, Inc., American National Rubber Company, Houdaille Industries, Inc., Huntington Alloys, Inc., Chemetron Corporation and Owens-Illinois, Inc. Mrs. Lucille Gillespie appeared for the Kanawha Valley Baptist Association, Clendenin, West Virginia, as a protestant. There were many protests.

Two witnesses were presented by intervenor, FMC Corporation; one witness appeared on behalf of low-income intervenors; one witness appeared on behalf of Owens-Illinois and one on behalf of Huntington Alloys, Inc.

On January 9, 1976, Appalachian filed its "Application for Interim Amendment to Appalachian's W. Va. P.S.C.

Tariff No. 3" requesting authority to credit .25074¢ per kilowatt hour for all service from August 28, 1975, through July 31, 1976. The reduction by "Rider A Credit Surcharge" (Original Sheet No. 18) resulted from the company's assessment that the embedded fuel cost component in the proposed rates should be reduced from 123.5¢ per Mbtu to 105¢ per Mbtu, and the application recited that the refund would include interest at 7¾% until paid.

On January 13, 1976, the Commission entered an order approving the application upon the condition, agreed to by Appalachian at a hearing held the same day, that the reduction in rates would continue until further order of the Commission, and would not terminate automatically on July 31, 1976, as proposed in the application.

Certain demand, energy and revenue data requested during the sessions ended August 31, 1976, were filed subsequently. Briefs were filed as to many of the issues before us, with the Appalachian's reply brief filed November 9, 1976.

Preliminary Comment

Background—Perspective

Appalachian is the largest public utility regulated by this Commission in terms of revenues received from West Virginia citizens. It brings the blessings of electric service to over 336,810 residential, commercial, industrial and institutional (churches and schools) customers located in 21 counties in the southern half of West Virginia. In addition, Appalachian is one of the main sources of power generation and transmission for the American Electric Power System, of which it is an integral part. The AEP system directly serves over 6 million customets [sic] in the States of Indiana, Ohio, Kentucky, Tennessee, Michigan, Virginia and West Virginia. Appalachian serves over 656,000 customers at retail in Virginia and West Virginia

and supplies wholesale electric service both within and outside of its retail market areas directly and indirectly by bulk transmission or displacement. This is done not only through the integrated AEP system, but also through 26 major electric utility supply systems which make up the regional grid known as the ECAR (East Central Area Reliability) group and through system inter-connected, non-ECAR electric utilities (TVA, Carolina Power & Light, Duke Power, Commonwealth Edison, Illinois Power, Central Illinois Public Service Company).

Other than distribution facilities, most of Appalachian's construction of generation, transmission and other facilities is planned on an AEP *system* basis of need and ***not*** solely on the needs of Appalachian Power Company customers. In addition, the construction of facilities by Appalachian and the said ECAR and non-ECAR electric utilities are planned on a coordinated, timed basis. The advantages of a coordinated group of power systems to the assurance of adequate, reliable and continuous public service are well known. Not so well known, however, is the fact that coordinated, "power center" controls over interlaced electric systems owned and operated by scores of cooperating affiliated and non-affiliated companies having generation capabilities, makes the fair, just and reasonable assignment of cost responsibility to various jurisdictions and classes of service a monumental regulatory task.

Background—Recent orders

On January 31, 1975, this Commission issued a comprehensive order allowing Appalachian a partial increase of requested higher rates on and after July 29, 1971, and providing for refunds. Since that date we have continued to regulate Appalachian to balance the interests of all segments of the public affected by its operations.

Highlights of this regulation progressed as follows:

On August 28, 1975, the Commission issued its order in Case No. 8192 denying Appalachian's request to impose a special surcharge on its West Virginia customers to recover unrecovered deferred fuel expenses occasioned by our order issued February 20, 1975, in Case No. 7945 terminating the automatic fossil fuel adjustment clauses in electric tariffs regulated by this Commission.

On October 10, 1975, we issued out interim order in Case No. 8235, which found that Appalachian had filed rates which resulted in an overrecovery of fossil fuel costs for the five-month period ended August 27, 1975, with the net overrecovery of $212,173 to be refunded in the subsequent Case No. 7083 (Reopened).

On October 20, 1975, we issued our order in Case No. 8229, denying Appalachian's attempt to exact a surcharge from its West Virginia customers alone to finance certain pollution control facilities at its Phillip Sporn generating plant.

On May 19, 1976, the Commission issued its order in Case Nos. 7083 (Reopened) and 8235, setting rates for the period January 1, 1974, through August 27, 1975, and providing for refunds. This set the lawful rates, underlying the proposed rates sought to be approved by this Commission in this Case No. 8182 for the period on and after August 28, 1975. See Appendix F, Column I.

As additional background to the foregoing Appalachian rate proceedings, this Commission on April 29, 1976, issued its certificate order in Case No. 8401, wherein Appalachian was authorized to construct a $72 million high voltage transmission line to move bulk power southeast from Cabell County to Wyoming County, West Virginia for eventual extension into its Virginia market area and beyond. Appalachian candidly admitted that its projected Culloden-Wyoming project would cause it to require

higher rates in the instant proceeding Case No. 8182. In our decision in Case No. 8401, we found that the appropriate apportionment of costs of this project to various rate jurisdictions and classes of customers for ratemaking purposes would remain an open question subject to determination in the appropriate rate proceedings.

The final backdrop to the rate drama now before us is our order issued September 15, 1976, in Case Nos. 7930 et al, which concerned certain of Appalachian's coal producing subsidiaries. We approved, with modifications, most, but not all, of the affiliated transactions as requested by Appalachian. However, we conditioned our modified approvals so as to be free in rate cases to be able to disallow excessive costs of purchases of coal produced by Appalachian's subsidiaries. This protection for Appalachian's West Virginia customers was found to be essential since the record in Case No. 7930, et al, indicated that beginning in early 1976, the price of affiliate coal in some months began to increase substantially above the price of coal purchased from non-affiliated suppliers, so that periodically the differential exceeded $3.00 per ton. We intend, in Case No. 8182 and future rate cases, to protect the public from excessive coal costs. In our said order in Case Nos. 7930, et al, we said:

> "In the circumstances of proven reserves and subsidiaries which are experienced in coal mine operations, there should be little reason for Cedar and Southern not to be able to sell their coal to Appalachian at a price lower than Appalachian is paying for coal purchased from its non-affiliated coal suppliers. In fact, except for bona fide *force majeure* occurrences, of which we are not aware, a continuation of such a differential in coal prices could lead us to conclude in an appropriate rate case that a higher coal price by affiliates is planned or is due to poor management.

> ". . . In the meantime, Appalachian should be induced by our present discussion of this issue to insist that its coal subsidiaries mine coal so as to sell it to Appalachian at the lowest possible reasonable price. Otherwise, Appalachain's [sic] payment of unreasonable coal prices to its affiliates must be absorbed by Appalachian as a deterioration of its earnings and will not be fully allowed as a recoverable item in its cost of service for rate-making purposes."

With these premises we turn to the task at hand of determining just, reasonable, and not unduly discriminatory rates for Appalachian covering the period beginning August 28, 1975, to the present and immediate future.

Issues

This proceeding contains the full sweep of usual rate case issues—rate base, allowable rate of return and going level and pro forma adjustments to operating expenses and other revenue deductions.

At the Commission's suggestion, the participants' [sic] attempted to narrow these issues by stipulation with only partial success, chiefly because of the threshhold [sic] issue of the propriety of using a 1974 test year to set rates beginning August 28, 1975.

The usual issues leading to a determination of over-all revenue requirements are supplementary to the equally complex issues of *jurisdictional* and *class* cost apportionment underlying the ultimate issue of proper rate level and rate design for the many different types of customers affected. The lowest possible reasonable revenue requirements [sic] is of immediate concern to the utility. However, West Virginia customers in each class are more concerned with how much *they* are going to pay as a fair share of Appalachian's total cost of rendering electric services to

the public located within and beyond the borders of West Virginia.

This Commission must *balance* these economic interests which pulsate with and against the meandering stream of the "public interest" in constantly changing patterns, much the same as the electricity flow which performs at the speed of light in amount, voltage and direction affected by billions of wise or wasteful human decisions to use or not to use power. Other regulatory bodies are called upon to perform these same tasks for the people within their jurisdictions. We now begin our difficult job to protect the interests of West Virginia with equity to all.

Test Year

On July 21, 1975, the evidentiary hearing began in Case No. 8182, together with Case Nos. 8192, 8235 and 7083 (Reopened). The rates in Case No. 8182 cover the most recent time period of the four cases that were consolidated, and is the sole remaining Appalachian rate proceeding now pending before this Commission.

At the outset of the first day of hearing in Case No. 8182, counsel for Appalachian agreed that its testimony presented on a 1974 test year would be the respondent's case on direct (T. 37-56). As the hearings progressed in 1975 to culminate in orders in the other three cases, the staff of the Commission performed its audit of Appalachian for Case No. 8182 on the basis of a 1974 test year.

On January 12, 1976, it was announced on the record (T. 529) that the staff's prepared testimony was to be served on the parties prior to February 24, 1976. In Case No. 7083 (Reopened), counsel for Appalachian recognized that "material must be audited" before final decision (T. 547). On the same day, at T. 562 and 564, the presiding officer stated:

> "We have begun to try the Case No. 8182 on a test period of 1974. The time has past for changing

> those test periods. The alternative of not sticking with this test period at this time when you are halfway through an evidentiary proceeding is that there would be a never ending rate case involving Appalachian Power if we were to permit this kind of leapfrogging of test year evidence and new test year we would never come to an end.
>
> ". . . and then if they want to protect themselves for the period beginning August 1, 1976, they have every right to come in here and file a new rate case which would then be heard on a test period that would be more applicable to that period."

On April 21, 1976, after the staff audit on a 1974 test year was completed, Appalachian sought to introduce evidence based upon a *1975* test year. The Commission refused to permit the company to deviate from its prior election to proceed on a 1974 test year, but left open the question of whether 1975 data would be admissible at the rebuttal stage of the hearing.

On August 10, 1976, the Commission adhered to its ruling that rates would be set on a 1974 test period, but admitted evidence based on a 1975 test period for the limited purpose of deciding the propriety of the adjustments made to 1974 test year data.

The Commission finds that its ruling was entirely proper, particularly in light of staff evidence based upon unaudited 1975 figures and proper adjustments, that there was no decline in rate of return on going-level projections for 1975 as compared with 1974. Moreover, Appalachian's unaudited 1975 data contained several improper adjustments. For example, it assumed approvals by this Commission which were not forthcoming, concerning the transfer of ownership of certain of its coal properties. We denied Appalachian's request to transfer such coal properties to its coal producer subsidiaries by order issued September 15, 1976, in Case Nos. 7930, et al. Also, in its 1975 test

year data, Appalachian adjusted its going-level expenses for both 1975 and 1976 wage and salary increases. This would render its 1975 projection incomparable to its 1974 test year data and would tend to understate the resulting 1975 rate of return.

As we have stated in the past, the selection of a particular test year to be used in ratemaking involves a discretionary judgment on behalf of the Commission.

When a utility seeks to depart from the test year it first elects to use in the evidentiary hearing for a more current 12-months period, the Commission must weigh the advantages of a more recent period against the disadvantages of delay in the administrative process required by a long recess for purpose of staff audit of the new period. In the instant case, as in our order issued May 19, 1976, in Case Nos. 7083 (Reopened) et al, we adhere to our ruling on a 1974 test year with limited reference to 1975 data, since we "must always protect the administrative process from abuse and bring rate proceedings to an end for the public good."

Due to the passage of time since the rates in question went into effect and the date of this order, we will fully protect Appalachian from any real or feigned unreasonable injury by setting rates in Case No. 8182 on a two-tiered basis — (1) for the period August 28, 1975, through April 30, 1976, and (2) for the period on and after May 1, 1976. Cf. *C & P Telephone Company, Case No. 7496,* order issued June 24, 1974, *W. Va. P.S.C. 61st Annual Report,* pages 204-224.

COMMENT

The starting point for our consideration of adjustments to test year 1974 costs is as follows:

	Per Books — Staff	
	Total Company	Allocated to West Virginia
Operating Revenues	$439,573,142	$187,641,566
Operating Revenues Deduction Operation and Maintenance Expense	$244,021,372	$ 97,757,987
Depreciation and Amortization	$ 40,357,524	$ 16,866,980
Taxes Other Than F.I.T. ...	$ 27,803,909	$ 15,138,692
Federal Income Tax	($ 191,105)	$ 1,907,377
Total Deductions	$311,991,700	$131,671,036
Net Operating Income	$127,581,442	$ 55,970,530
Average Rate Base	$1,131,301,490	$472,790,666
Rate of Return	11.28%	11.84%

Appalachian's evidence of per books costs differed from the results of the staff's more recent audit made after accounting adjustments for federal income tax expense and differences in jurisdictional allocations of costs to West Virginia. Moreover, Appalachian's rate base methodology was not comparable to that of the staff, thus distorting the comparability of resultant rates of return both before and after going-level and pro forma adjustments of staff and company.

The end result after various adjustments to a going-level by Appalachian and staff compare as follows:

	APPALACHIAN		STAFF	
	Total Company	Allocated to West Virginia	Total Company	Allocated to West Virginia
Adjusted Operating Revenues	$ 425,550,313	$180,880,505	$ 420,827,187	$176,085,074
Adjusted Operating Rev. Ded.				
Operation and Mn. Expense	$ 257,133,668	$ 96,120,982	$ 263,751,098	$105,990,991
Depreciation and Amortization	$ 46,364,714	$ 20,894,282	$ 41,558,747	$ 17,334,859
Taxes Other than F.I.T.	$ 31,608,703	$ 17,166,935	$ 30,829,056	$ 16,023,424
Federal Income Taxes	$ 11,270,218	$ 6,730,704	($ 1,893,176)	($ 737,846)
Total Deductions	$ 346,377,303	$140,912,903	$ 334,245,725	$138,611,428
Net Operating Income After Adjustments	$ 79,173,010	$ 39,967,602	$ 86,581,462	$ 37,473,646
Allowance for Funds Used During Construction	$ 4,672,345	$ 2,142,040	—	—
Total Operating Income Plus Allowance For Funds Used During Construction	$ 83,845,355	$ 42,109,642	$ 86,581,462	$ 37,473,646
Rate Base	$1,319,121,055	$595,076,068	$1,171,404,899	$488,448,552
Rate of Return	6.36%	7.08%	7.39%	7.67%

The staff going-level rate of return of 7.67% for West Virginia is calculated on an *average* rate base, while the Company's going-level rate of return of 7.08% is based upon a *year-end* rate base, plus full allowance for plant expenditures accounted for as Construction Work in Progress (CWIP), and the addition of an income allowance for funds used during construction (AFUDC).

Specific Adjustments

The foregoing indication of wide divergence in the positions of Company and staff must be resolved by decisions on several specific, subsidiary issues to reach a representative matching of allowable costs to projected test-year revenues to set rates for the periods beginning August 28, 1975, and May 1, 1976.

Since we have decided that 1974 is an appropriate test year to use in the circumstances of this case, we interpret Appalachian counsel's letter to staff counsel dated August 10, 1976, as an agreement to narrow certain specific issues to be decided to the following:

1) Allowable adjustment to going-level fuel expense and related revenue adjustment.
2) Adjustment to purchased power expense to offset effect of an obsolete Capacity Equalization Agreement among affiliates of the AEP system.
3) Depreciation expense—(a) certain anti-pollution plant and (b) rights-of-way.
4) Property tax expenses in three States.
5) Miscellaneous adjustments for 1976 expenses.
6) Rate base—(a) working capital, (b) year-end vs. average and (c) Construction Work In Progress.
7) Rate of return on rate base.
8) Federal Income Tax—(a) normalization-tax depreciation, (b) investment tax credit—level

and normalization, (c) consolidated tax savings and (d) pro-forma revenue tax effect.

9) Jurisdictional cost apportionment.

10) Class of service cost apportionment.

11) Rate level and rate design.

1. *Adjustments Related to Fuel Expense*

One of the most difficult and substantial issues in this case is the determination of a reasonable level of fossil fuel expenses for the test year to set rates for the periods which began August 28, 1975, and May 1, 1976.

Appalachian urges a going-level *fuel* expense at $1.05 per million Btus *estimated* as the average for the period March 1976 through December 1977, which period began six months after the date the proposed rates were put into effect. Staff presented evidence to support an adjustment of *coal* expense to $221,257,082 (at $.998416 per million Btus) based upon the period September 1975 through April 1976, which period began eight months after the end of the test period and covered the immediate eight-month period after the requested rates were put into effect under bond. The effect of this staff adjustment would be to reduce actual test year per books coal expense from $225,966,126 (at $1.01966 per million Btus) to $221,257,082. These costs are for coal expenses only and are not the total Account 501 fuel expense, which includes other fuel and handling expenses. The comparable staff weighted average total Account 501 unit cost would be about $1.02 per million Btus.

We find that $1.00 per million Btus is a reasonable level of coal expense for determining the *first-tier* rates covering the period August 28, 1975, through April 30, 1976. In our order issued October 10, 1975, Case No. 8235, we found that the actual unit fuel cost for the period April through August 1975, was $1.03604 per million Btus. Coal prices

declined and stabilized somewhat in mid-1975. Thus, by adopting the staff approach the customers of Appalachian are given the benefit of the recent "softening" in the coal market.

Appalachian's proposed adjustment to $1.05 per million Btus is rejected, because rates based on such "estimated" fuel costs would permit Appalachian to recover substantially more than its actual fuel costs for that eight months period in which the first-tier rates are made firm.

However, for the purpose of determining *second-tier* rates for the future on and after May 1, 1976, we cannot ignore the relentless march of inflation on the price of coal. As disclosed by the record, we monitor the price of coal (Account 151) through the monthly fuel reports filed by Appalachian under Code 24-2-14. We have noted that beginning in the last two months of 1976 and the first two months of 1977, the price of coal purchased from non-affiliated suppliers is increasing, possibly due to wage escalations under the UMWA union contract.

The evidence of record indicates that the 1974 test year cost of affiliated coal was *lower* than non-affiliated coal purchases. This relationship has now reversed so that affiliated coal is currently *higher* than "outside" purchases. As previously stated we have warned Appalachian that we would protect the public from excessive coal costs. In Case Nos. 7930, et al, by order issued September 15, 1976, we cautioned Appalachian that it may be made to absorb any unreasonable differential between the price it pays for coal to its affiliated suppliers and to its non-affiliated coal producers.

However, we need not go outside the record to determine a reasonable level of fuel expense for setting rates to be lawful on and after May 1, 1976. In our judgment, based on the evidence, confirmed by our analysis of monthly fuel reports under Code 24-2-14, we find that $1.04 per million Btus or $230,472,530 is a reasonable level of coal expense

to be allowed in the costs to be recovered by the *second-tier* rates. This is greater than Appalachian's actual 1974 test year coal expense of $225,966,126.

Counsel for Appalachian objected to staff's *revenue* adjustment No. 3, which reflected the "roll-in" to base rates of .998¢ per KWH occasioned by our termination of the fuel adjustment surcharge as of April 1, 1975. Appalachian appears to argue that the going-level fuel cost adjustment should be $1.05 per $\overline{M}$Btus, rather than $.998416 $\overline{M}$Btus, and if so, the revenue adjustment would be erroneous. Such an objection is not well taken, because we are here considering a going-level adjustment which the staff made in order to reflect rate levels in effect prior to the filed rates proposed herein. Our allowance of $1.04 per $\overline{M}$Btus for the second-tier rates will increase expenses and any revenue deficiency resulting from higher fuel expenses will cause a resultant increase in allowable revenues to cover the higher costs.

2. *Purchased Power Expense Adjustment to Reflect Effect of Renegotiated Capacity Equalization Agreement Among AEP Affiliates*

The affiliates of the AEP system are each in different stages of growth. By virtue of the fact that growth of steam generation is on a *system*-basis rather than a *company*-basis, excess capacity on one AEP company is made available to its sister companies on a shared basis pursuant to agreement setting up a formula rate, allocating portions of the operating and capital costs of the excess capacity. This agreement among affiliates is known as the "Capacity Equalization Agreement". It is regulated by the Federal Power Commission.

During the test year Appalachian was a capacity-excess company and received revenues from its sister companies based in part upon a formula which contemplated an unreasonably low investment per kilowatt of generating capacity ($100 per KW of capacity) as compared with the

actual investment of in excess of $150 per KW of capacity during 1974. The AEP companies recognized this underpricing and in June 1975 filed with the FPC its Modification 3 to the Capacity Equalization Agreement.

Recognizing a need for going-level adjustment to power production expense on a known and measurable basis, the staff adjusted test year per books power production expenses by crediting revenues of $30,873,058 from AEP affiliates, instead of $26,209,579, against total power production expenses of $227,940,896, for allowable power production expense $3,939,615 less than it would have been otherwise.

The Company contends that the staff adjustment is improper not because the capacity equalization rate had been increased in June 1975, but because at some point subsequent to the test year Appalachian purportedly became a capacity-deficient company in the AEP system. The Company's contention is not well taken, because even when it is a net purchaser of power from its affiliates at a higher capacity equalization rate, it will have the benefit of substantial increased revenues from the resale of its purchased power under the Capacity Equalization Agreement.

It may well be that the Modification 3 rate formula provides charges which are still too low as among affiliates. This could be determined after cost apportionment studies. No cost apportionment studies were presented in the record going to classes of service within the Federal sphere of jurisdiction. However, since the AEP companies filed the Modification 3 rate formula with the FPC, Appalachian could not argue that the staff adjustment was excessive or was not based on a known and measurable change occurring soon after the end of the test period.

We find that the staff adjustment to per books purchased power expense to reflect a going-level reduction caused by an understatement of capacity equalization revenues is proper and reasonable.

3. *Depreciation Expense Adjustments*

Pollution Control Facilities

In late 1974 and 1975, Appalachian added pollution control facilities to its Glen Lyn and Clinch River generating plants. On the basis of an investment of $39,741,706 at August 31, 1975, staff would allow an adjustment to depreciation expense of an additional $1,231,993, derived from applying a 32-year service life or a depreciation rate of 3.1% to the investment.

The Company, on the other hand, urges the Commission to allow a depreciation expense adjustment, at much higher depreciation rates, amounting to $5,008,508 derived from the estimated remaining lives of the respective generating units to which the electrostatic precipitators are attached varying from 3 years remaining life for Glen Lyn Unit No. 5 to 21 years for Clinch River Unit No. 3.

This Commission has refused to permit utilities to increase their depreciation rates and expense in contemplation of a rate case. See *Cabot Corporation, Case No. 8289,* order issued October 6, 1976, at page 10. Changes in depreciation rate may be proper in order to protect invested capital which is subject to rapid physical deterioration, obsolescence or functionally reduced service life. However, there is always the temptation for a utility to increase its depreciation rates in order to attempt to justify an increase in rates and charges to its customers. For this reason, in our new Rules of Practice and Procedure dated March 1, 1977, we have adopted Rule 20 covering changes of depreciation rates, so as to ease the problem of how to reconcile accounting changes required by good engineering, accounting and management principles, with proper ratemaking. The intent is to establish proper depreciation rates prior to and independent of ratemaking to the extent permitted by the circumstances.

Staff argues persuasively that Appalachian's position is too extreme, because, for example, it would assume unrealistically that Appalachian would have spent $7,000,000 in 1974 for anti-pollution devices on its Glen Lyn Unit No. 5 and would retire the same from service early in 1977.

We find that the staff position is proper and that Appalachian has failed in its burden of proof to establish depreciation rates which are higher than the 3.1% composite generating plant depreciation rate used by the company for the units to which the electrostatic precipitators are attached.

Rights of Way

Appalachian seeks our approval for an adjustment to its depreciation expense by an additional $1,010,000 for depreciation on transmission rights of way and distribution rights of way. Traditionally, land, including rights of way encumbering realty, are not depreciable, for other than tax or special statutory purposes in certain circumstances. There is nothing of record to support the Company position on this issue. The claimed depreciation expense does not fall within any tax or special statutory exception to the general rule excluding rights of way from depreciation expense accounting. To the contrary, the claimed depreciation expense has never been recorded on Appalachian's books and the record is silent on the nature of the rights of way, their estimated service life and the method of reaching the claimed depreciation expense. We find that Appalachian's claim for depreciation expense adjustment is without merit and is rejected.

4. *Property Tax Expense Adjustments*

In Appalachian counsel's letter narrowing the issues in controversy, he took the position that regardless of whether the test year would be 1974 or 1975, "property taxes should reflect *actual* taxes paid in *1975*". However, this issue was not briefed by Appalachian. Pertinent evi-

dence shows real and personal property taxes to be as follows:

	1974		1975
	Per Books	Staff Adjusted	Per Books
West Virginia	$5,237,110	$ 7,405,577	$6,483,804
Virginia	3,922,844	5,229,582	3,431,101
Tennessee	31,542	34,128	36,647
Total	$9,191,496	$12,569,287	$9,951,552

We have selected 1974 as the test year and will approve the staff adjustments as made. The per books property taxes are as shown due to Appalachian's overaccruals of property taxes for prior years.

Property taxes are only one type of tax accounted for as "Taxes Other Than Federal Income". Other taxes, such as payroll taxes, gross receipts or business and occupation taxes and regulatory fees, will be further adjusted to reflect the effect of wage adjustments allowed in setting the second-tier rates to be approved, increases in the FICA tax base and revenue adjustments derived from the rates determined herein.

5. *Second-tier Miscellaneous Adjustments For 1976 Going-Level Adjustments To Expenses*

Because of the unique regulatory background involving Appalachian before this Commission and the necessary passage of time to afford full due process of law in our actions in this case, we are adopting the rare procedure of setting two different levels of rates in one numbered proceeding before us. We have already disposed of the most substantial subsidiary issue by finding above that the embedded cost of coal for determining rates to be in effect on and after August 28, 1975, through April 30, 1976, should be $1.00 per $\overline{M}$ Btus, and for the period on and after May 1, 1976, should be $1.04 per $\overline{M}$ Btus.

In addition, Appalachian urges that a going-level adjustment be made to the 1974 test year for (1) wage and salary increases put into effect April 1, 1975, and April 1, 1976; (2) postage rate increases which went into effect December 28, 1975; (3) medical insurance premium increases that took effect March 1, 1976; and (4) an FICA tax base increase effective January 1, 1976.

The record reveals that the magnitude of these additional operating expense adjustments would be as follows:

	Total Company
(1) Annualized Wage and Salary Increases:	
— effective April 1, 1975.....	$1,823,000
— effective April 1, 1976.....	2,684,000
(2) Postage Rate Increase.....	248,000
(3) Medical Insurance Premiums.....	343,000
(4) Increase in FICA Tax Base.....	181,000
Total	$5,279,000

In addition, a fifth adjustment was proposed by Appalachian of $1,531,000, representing a restoration of line maintenance expenses which were cut back in 1974, as an austerity measure to minimize cash outflow and to improve earnings. The test year expense reductions which should be restored to assure adequate service were detailed as follows:

80 line crews (412 men), outside contractors used in —ground line pole treatments	$ 187,000
— pole and tower painting	54,000
— overhead line maintenance	576,000
47 crews (147 men), outside contractors used in — tree and brush control.....	600,000
Related maintenance material costs.....	114,000
Total	$1,531,000

These five adjustments are found to be reasonable and proper and based on evidence establishing known and

measureable criteria and are to be allowed in determining the *second-tier* rates to be in effect on and after May 1, 1976. The April 1, 1976, wage increase, postage rate increase, medical insurance premium, and increase in FICA tax base are *not* allowed for the rate determination underlying the period August 28, 1975, through April 30, 1976, because their cost impact would not be substantial until the second-tier period.

We will allow for both the *first-tier* and *second-tier* periods and adjustment to the 1974 test period costs to reflect the annualization of wage increases that became effective April 1, 1975, in an amount of $1,823,000, and was recommended by staff as a proper going-level adjustment.

The adjustment of $1,531,000 in line maintenance expense, recommended by staff in its Exhibit No. 8, is allowed in both the first-tier and the second-tier rates so that in the future Appalachian will not be able to rely on a temporary austerity program to defer proper and necessary line maintenance required for adequate service to the public.

These adjustments are unusually liberal to the Company and are allowed in the determination of rates as described only in the context of the circumstances of this case affecting Appalachian and its customers. It is but one factor affecting our judgment, while realizing that such will be counter-balanced by our decisions on other subsidiary issues so that the end-result in rate-making will be fair, just and reasonable to all concerned.

6. *Rate Base*

This Commission has pointed out that "rate base", better described as "earnings base", is significant in ratemaking only as a tool to determine "allowable earnings" for a test period. In the "rate base—rate of return" method of ratemaking, the "allowable earnings" is the resulting product from the multiplication of "rate base" times "rate of

return". The allowable earnings are needed to retire debt, pay interest and dividends, and otherwise to be used in the business for construction or working capital. Such allowable earnings should also be adequate to permit the utility to finance reasonable expansion. Said "allowable earnings" are then subject to increase to recover "projected" income taxes associated therewith, by inclusion in the total cost of service to be recovered by the rates to be designed.

Except as to certain very small utilities and some governmental utilities, the "rate base—rate of return" method is the usual mode of cost-based ratemaking. This method uses projections of reasonable capital costs as but one component of the total reasonable costs (revenue requirements) allowed. The "end result" of just and reasonable rates are based upon these reasonable test year revenue requirements.

Although we discuss the two factors of "rate base" and "rate of return" separately and in precise numbers, we do so with an understanding of the limitations and interrelationships of certain concepts which affect our judgmental decisions. Evidence on the issues of rate base and rate of return are susceptible to a range of findings all of which have validity. Since the important consideration is the product of the two factors, rather than the factors themselves, our judgment in selecting precise numbers within a range of acceptable numbers are interdependent. Thus, there is a need to be fully aware of certain distinctions and the nature of statistical evidence. For example, there is a difference in concept and often a substantial variance in dollars between "rate base" and "total capitalization". "Rate base" consists of net plant (less customer contributions and tax deferrals) plus an allowance for working capital; whereas, "total capitalization" includes debt, deferred equity and common equity. Distinguishing these concepts, Appalachian's witness Brennan can show an actual, year end *total capital* of $1,397,451,000 as of Decem-

ber 31, 1974, and its witness Berg can sponsor a per books, year end *rate base* of $1,318,019,244, without being inconsistent. See Appendix A to this order. Likewise, it is not inconsistent for rate base witnesses to make going-level adjustments to change the test year rate base to another amount for purposes of fairness on the "matching" principle. It is partly for this reason that results of rate of return on capitalization studies are not the same as rate of return on rate base.

The concept of test year projections and adjustments to rate base costs, costs of service and revenues in *ratemaking* is a theorization based on facts in an attempt to reach a fair ideal matching of costs to revenue for the immediate future in order to prevent either excessively high or unreasonably low earnings. The Commission now and in the past has used such projected data in this fashion.

Proceeding now to the specific controversies over rate base items in this case, the Company urges as to (1) use a "year-end" rate base rather than a 13-month "average" rate base, (2) include in rate base *all* expenditures accounted for as "Construction Work in Progress" (CWIP), and (3) include in rate base an amount for cash working capital based upon an allowance of 1/8th of test year operating and maintenance expenses, excluding purchased power expense, but unadjusted for the lag experienced in payments for coal purchases.

The Commission has adhered to the average of 13-month balances method of ratemaking and the exclusion from rate base of most Construction Work in Progress, because it believes that the test year method of ratemaking should attempt to properly match the relationship between plant, expenses and revenues. We have allowed an exception to the general principle which excludes CWIP from the rate base in the case of CWIP expenditures for pollution control facilities, because such expenditures are (1) large, (2) required by governmental environmental regulation, (3)

non-revenue producing, and (4) operating cost increasing. The exception is made because of the equities involved and the same matching principle that supports the general rule. Such limited CWIP is allowed in rate base, so that the utility will be allowed to begin immediately to recover from ratepayers for substantial expenditures made involuntarily by the utility in compliance with governmental edict.

Both the year-end rate base and CWIP recommendations by Appalachian are rejected because, in the context of a substantial growth company, they tend to unduly accelerate the recovery of costs by mismatching capital costs for plant, which is just beginning to be or will be "used and useful" in the rendition of utility service, with test year billing units applied to adjusted revenues and costs.

In a growing company such as Appalachian, a *year-end* rate base would be larger than a rate base determined on an *average* monthly basis. The Staff shows a per books *average* rate base for 1974 as $1,131,301,490 to be adjusted to a going-level of $1,170,149,735 for total company.

Obviously, *any* allowable rate of return would produce higher earnings on a year-end rate base than on an average rate base for ratemaking purposes. As to a company with substantial growth in plant and sales, allowance of year-end rate base and *all* CWIP in rate base would tend to skew unreasonably a fair and representative relationship between revenues derived by application to lower test year billing units and higher capital costs for plant growth needed for greater future sales.

The Staff argues that exclusion of most CWIP from rate base is fair, since the Company can capitalize an Allowance for Funds Used During Construction (AFUDC) and recover such funds, including a return thereon, when the construction projects are completed and placed in service. Construction Work In Progress is a plant asset item on the balance sheet with no specifically related counter-entry in the total capitalization, either as debt or equity. The real

question is the extent to which present customers or stockholders should carry the burden of these CWIP expenditures for service to begin at some unknown date or dates in the future. We find that the Staff positions on these two subsidiary rate base issues are sound. We adhere to our prior precedents which require an average rate base, adjusted for year-end Construction Work In Progress dollars invested in pollution control facilities.

The working capital rate base issue is presented to us in the following manner. It is a standard principle that a utility should be allowed to earn a return on a reasonable level of cash working capital.

Working capital is not a constant or fixed percentage of rate base. Although it is sometimes approximated by formula or percentages, such mathematical exercises are valid only as an administrative convenience to be modified when results tend to be disproportionate under a fair analysis. Working capital is composed of three major components. The test year per books amounts as adjusted by Staff are as follows:

	Per Books		As Adjusted	
	Total Company	Allocated To W. Va.	Total Company	Allocated To W. Va.
	$	$	$	$
Materials and Supplies (Inc. Fuel)	63,051,604	25,224,455	63,051,604	25,224,455
Prepayments	985,651	408,848	985,651	408,848
Working Cash	15,362,671	6,290,961	19,810,607	8,059,853
Total Working Capital	79,399,926	31,924,264	83,847,862	33,693,156

The cash working capital component may be defined as the amount of cash required to be available to a utility for the payment of its operating and maintenance expenses which are incurred and paid for before operating revenues are sufficient to pay for such expenses. Theoretically, the investor is providing this cash for a short period of time

before the customer receiving service pays revenues to cover the expenses inherent in the service. The investor is allowed to earn a return on his investment used by the utility as cash working capital. Thus, the reason for the rule is tied directly to the lag period between the average time expenses are incurred and paid and the average time concomitant revenues are received by the utility. It can be argued that a regulatory body should be generous in allowance for cash working capital in rate base, in view of the fact that a utility has the legal obligation to perform continuous, adequate service to the public and cannot shut down and refuse to buy electricity or generating fuel to lessen the need for cash working capital. However plausible this argument, this West Virginia Commission must be neither generous nor niggardly, but must seek a balance and fair decision on this issue, as well as all issues, that affect the public servant and the public served.

In the past the Commission has used a modification of the FPC 45-day formula, whereby it has allowed as cash working capital 45/365 or ⅛ times the total operation and maintenance expenses after deducting purchased power expense. Purchased power expense is deducted on the premise that it does not represent an immediate cash outlay or does not have to be paid until close to or after the amounts involved have been collected from the customers.

In some cases, the Commission has allowed the utility to include fuel expense in the operating expenses to which the ⅛th factor is applied on the premise that there is a 45-day lag between the payment for the fuel and the receipt of revenues for the sale of electricity generated by the fuel. However, fuel expenses is [sic] such a large part of total operating expenses, that we should constantly review each utility's purchase and payment for fuel and receipt of concomitant revenues, to ascertain whether in fact a 45-day cash working capital requirement is realistic.

In this case, the staff audit revealed (based on August 1974 coal deliveries) that the Company was receiving revenues for service from 30 to 60 days after service, for an average of 45 days, while it was paying for coal purchased on an average of 29 days after it received the coal. Thus, deducting 29 days from 45 days, there would be a 16-day lag period during which the customer's money would not be available to pay for the fuel portion of service received. Therefore, Staff's adjustment to cash working capital was calculated upon a 16/365th, instead of a 45/365th or 1/8th, of fuel expense to reflect a lesser need of invested cash.

For these reasons we accept the staff methodology of calculating a reasonable allowance for working capital to be included in rate base.

7. Rate of Return

Cost of capital on Appalachian's *total capitalization* is but one of several guidelines to the Commission's judgmental decision on rate of return to apply to *rate base* for ratemaking purposes. We have previously discussed the differences in concept and dollars between (1) "total capitalization" used to estimate cost of capital and (2) "rate base—rate of return" in ratemaking. Thus, it would be improper to believe that a regulatory body would be bound by a rigid mathematical calculation of weighted average cost of capital based upon total capitalization, for purposes of setting a rate of return on rate base. In 1975 and 1976, the Commission set rates for Appalachian based upon an 8.73% rate of return to be applied to a 13-month average rate base for West Virginia. Not too many decades ago, in an era having low inflation, rate of return was not a major item to be litigated in ratemaking. It was recognized then that 6% was a fair, just and reasonable rate of return to be allowed by regulatory bodies. Utilities planned their growth, financing, and operations accordingly. During this period, utilities were able to grow at a reasonable pace to meet their public service obligations and

prosper. Within the past quarter of century, however, inflation and dislocations in the economy, due to such things as widespread and substantial governmental deficit spending, have increased the cost of capital, which, in turn, has affected a steady increase in rates of return allowed on rate base in ratemaking. We trust that there is a point in the not too distant future when the government and the governed will realize spiralling inflation must be stopped and take steps to do so, so that utilities will grow and serve the public within the limits of a non-increasing rate of return on rate base.

Looking first at the cost of capital criteria for determining rate of return, we find that Appalachian seeks a rate of return on year-end rate base in the range of from 9.65% to 10.1%. Appalachian would translate cost of capital expressed in percentage of total capitalization to rate of return on rate base with no other considerations. Moreover, Appalachian would have us believe that the calculated weighted cost of capital is a fixed and proper rate of return, regardless of the rate base to which it is applied. This is not true when one considers the many variances possible in arriving at an allowable rate base. Thus, both the cost of capital and the methodology employed in arriving at rate base must be considered before a fair rate of return can be determined. The Staff cost of capital witness followed the same basic error of believing in strict translation of cost capital into rate of return on rate base. On this basis staff recommended a 9.42% rate of return based upon evidence of cost of capital at December 31, 1975, of from 8.75% to 9.16%, and cost of capital estimated at December 31, 1976, to range from 9.17% to 9.67%.

An equally important consideration in determining rate of return is the necessity for higher earnings. If higher earnings are needed for improvident or excessively accelerated expansion or for excessive return to the common equity owners, the requested rate of return would be too high.

Here, however, Appalachian carried its burden of showing a need for rate of return higher than the 8.73% previously allowed, albeit not at the levels requested. Appalachian presented evidence that its senior securities and commercial paper had been downgraded to be at the lowest rating of all of the major electric utilities in the country. It argues that its debt coverage is dangerously low, so as to limit its ability to finance growth needed for its generating and transmission capacity. Appalachian argues that it needs higher rates to restore to a normal construction level its project 1300 megawatt generating unit partially completed at its site in New Haven, Mason County, West Virginia. In Case No. 8401, by order issued April 29, 1976, this Commission certificated Appalachian's 765-kV high voltage transmission line to run from Culloden in Cabell County to Wyoming County, West Virginia, while recognizing that Appalachian contended that it needed rate relief in Case No. 8182 in order to construct the $72 million project. Appalachian estimates its 1976-1980 construction program will require up to $1.3 billion, which would average $260 million per year. A portion of this financial requirement will be generated internally, with the balance raised from investors. In either case, Appalachian will require an improvement in earnings to be able to continue a reasonable growth to satisfy the electricity demands of an energy-short public.

There are several considerations, however, which militate against allowing a rate of return as high as is recommended by Staff or by Appalachian. First, the Commission has been liberal in its allowance of adjustments to fuel expense and other expenses for the second-tier rates. Second, we have permitted a measure of CWIP in rate base. Third, as discussed below, we are allowing a partial normalization of federal income taxes in order to improve the quality of earnings and to encourage growth of plant. Fourth, we have grave reservations about whether or not

West Virginia is paying its proper share of total costs vis-a-vis sales by Appalachian subject to other regulatory bodies as discussed below. Finally, the customers of Appalachian in West Virginia are not able to give it *carte blanche* for unlimited rate increases which cannot be absorbed by their limited incomes.

In the light of all of these considerations and the evidence, the Commission finds in its judgment that the allowable rate of return on rate base for Appalachian in this case is 9.35% for West Virginia.

It is hoped that Appalachian will be able to reduce unnecessary or unreasonable costs—such as (1) its cost of coal purchased from its affiliates and (2) other Account 501 fuel costs—in order to earn *more* than 9.35% on total capitalization. The actual results of future fiscal periods will reflect the good or bad results of management decisions, increased sales volumes, and efficiencies that will come with additional modern generating units and high voltage transmission systems. By keeping rates at levels which will recover no more than the lowest possible *reasonable* level of test year costs, we regulate in a balanced way to induce management to search for cost reductions, prudent growth, and greater efficiencies in operations.

8. Federal Income Tax Expense

As a general principle, a public utility must be allowed rates high enough to generate revenues sufficient for it to pay its federal income tax liability. It seems only just that public utilities pay their fair share of the cost of our federal government. Moreover, when a Company seeks and secures a rate increase, it would usually be expected that its greater revenues would result in higher earnings and, therefore, a higher income tax liability. However, under current federal income tax laws, this is not always the fact.

In Appalachian's situation it can generate millions of dollars of earnings which are subject to very little or no income tax liability because of Congressional modification of the tax laws which have accomplished the following:

(1) Profitable members of a public utility holding company system can enjoy tax savings due to the election by all of the members of the system to file a consolidated income tax return through their parent corporation, under Section 1501 of the Internal Revenue Code.

(2) Public utilities are allowed tax credits reducing their federal income tax liability in varying percentages of investments in public utility property, depending upon (a) the dates of installation, (b) the nature of the property, such as pollution control facilities, (c) the mode of rate regulation by regulatory bodies having jurisdiction and, (d) timely accounting and tax elections by the regulated utilities, all under Sections 38, 46 through 50 of the Internal Revenue Code.

(3) Public utilities are allowed accelerated depreciation and amortization deductions from gross taxable income at higher levels than booked under the straight line depreciation method used for certain depreciation expenses for non-tax purposes, depending upon (a) the dates portions of the property are placed into service with reference to pre-1970, post-1969 and facilities in operation before 1976 requiring pollution control additions, (b) timely accounting and tax elections by the regulated utilities and (c) the manner of rate regulation by pertinent regulatory bodies having jurisdiction, under Sections 167 and 169 of the Internal Revenue Code.

The history of the underlying tax statutes reveals the attempts of Congress to reconcile the interplay of two principles. First, there was the Congressional attempt to stimulate the economy by tax concessions to businesses to

encourage growth of tangible capital assets. Second, there was Congressional vacillation from time to time between attempts to limit and attempts to assure the benefits of tax concessions to public utility business enterprises. In so doing some states believe that these Federal tax laws threaten to cause an incursion by the Federal Internal Revenue Service in the ratemaking processes which are the jurisdiction of State regulatory bodies. The potential conflict between the Federal IRS and certain State regulatory bodies is materializing in California, where that State is reducing utility rates in a way that, under Section 46(f) of the Federal income tax law, certain California utilities may lose their tax credits and earlier tax savings and be assessed huge amounts of additional taxes.

Our West Virginia Public Service Commission need not and will not involve itself in this case in the type of controversy that is brewing in California. Appalachian has demonstrated that it needs substantial moneys from (1) earnings, (2) tax savings or deferrals, and (3) the financial market to be able to invest in new or expanded generating, transmission, and other facilities to be able to render adequate service to its broad market. Moreover, all parties to this proceeding concede that this Commission can grant, withhold, or modify its allowable Federal Income Tax expense and accruals to be used in the cost of service and rate base for ratemaking purposes in relation to normalization, averaging, or other methods of ratemaking, so long as this Commission does not "plainly contravene" the statutory scheme and the precise limitations of the Internal Revenue Code where Congress has failed to give rate regulatory bodies a formula to follow. *F.P.C.* v. *United Gas Pipeline Co.*, 386 US 237, 87 SCt 1003, 68 PUR3d 321.

Appalachian has elected to participate in the benefits of consolidated tax savings and investment tax credits and now seeks to switch from "flow through" to "normalization" accounting and ratemaking for certain, but not all, of the

tax benefits that result from adopting available tax depreciation methods which provide greater early year tax deductions and, therefore, less current income tax liability than would be derived from using booked straight line depreciation for tax purposes.

The Commission's discretion in determining an allowance for federal income tax expense in ratemaking must start with the fact that a projection of test year pro forma revenues, expenses and rate base cannot be an exact forecast of the immediate future after a rate adjustment is allowed. This is particularly true with respect to Federal Income Tax expense, because too many variables are involved, some of which are within and some outside of the control of the utility. For example, tax credit rates are changed by Congress; the taxpayer can switch his options to minimize his tax over several tax periods; qualified public utility properties can go into service at accelerated or delayed dates at management election; carryback and carryover of unused tax credits can distort the matching periods of expenses and revenues, and tax audits by the Internal Revenue Service can substantially change a utility's actual tax liability several years after the tax period.

As we stated in Case No. 8000, Columbia Gas of West Virginia, Inc., order issued June 16, 1976:

> "An informed judgment to determine an allowable federal income tax component in a cost of service for ratemaking purposes is a substantially different thing than calculating the actual taxes to be paid by a utility in its annual tax return. When regulatory bodies and reviewing courts say that only 'actual taxes paid' should be allowed in the cost of service for ratemaking purposes, they are enunciating a broad, general principle, which has certain limitations which must be fully understood when the principle is applied."

We start now with our findings on each subsidiary Federal income tax issue to be sure that they are based on rational criteria.

A. Consolidated Tax Savings

Appalachian agrees that tax savings derived from filing a consolidated tax return by its parent, American Electric Power, Inc., should be *shared fairly* with Appalachian's West Virginia customers. Appalachian contends, however, that the portion of tax savings due to the losses of the parent corporation should not be used in the formula for determining consolidated tax savings. The net effect of the Company position would reduce the average of consolidated tax savings percentages as compared with the results of separate tax filings, so as to reduce the consolidated tax savings and thereby increased the Federal income tax expense to be recovered as part of the total cost of service used in ratemaking. Appalachian would impute to itself the portion of its parent corporation's tax loss benefit derived by the percentage which Appalachian's taxable net income bears to the total taxable net income of the taxable net income companies. Staff, on the other hand, would calculate consolidated tax savings on the basis of including parent company losses with the other elements that create a consolidated tax savings and would apply a percentage reduction for consolidated tax savings to pro forma taxable income. Appalachian contends the consolidated tax savings should not be increased as incrementalized to pro forma taxable income and that the test year tax savings should be $664,371, instead of the $4,100,837 tax savings allocated to West Virginia.

Staff has followed long-standing Commission precedents in its method of estimated consolidated income tax savings, which have a rational basis. The Company method is not shown by the record to have any greater validity. Because

of the variables involved and the inherent imprecision in projecting a test year pro forma income tax allowance, the staff evidence based on historical facts of consolidated tax savings over a three-year averaging period (1971-1973) is found to be reasonable.

B. Investment Tax Credits (Job Development Credit)

The calculation of investment tax credits for a public utility's Federal income tax return is a most complicated task. Appalachian has been "flowing through" tax savings from the investment tax credits, which were 3% in 1962-1968, 4% in 1971-1974, and 10% starting in 1975. The tax credits are derived by multiplying these percentages times qualified investments in public utility facilities placed in service in the appropriate years and increased, if elected, by 3-year carryback and 7-year carryover of unused tax credits. There are other complexities; such as, "transitional rules" for the period between January 21, 1975 and January 1, 1981; limitations on the magnitude of the tax credits, and variable percentages of aggregate qualified investments of varying service lives in tax years 1975-1980. Suffice it to say that projecting an estimate of investment tax credits for the immediate future, as represented by a pro forma test year, which will approximate the *actual* investment tax credits to be realized is purely a matter of regulatory judgment and discretion. In these circumstances, the averaging method of projecting an estimate of the tax credits is a conservative way of determining a fair reduction in allowable Federal income tax expense.

Appalachian attacks the Staff method of using a 5-year average, rather than a 3-year average, without a maximum 90% limitation. Appalachian claims that the 5-year period includes qualified investments arising from its additions at its Amos plant, and that this unreasonably inflates the tax credit base used in the averages. The Company points

to its investment tax credits (unaudited by IRS) of $2.6 million in 1974, $4.4 million in 1975, and estimated $8.3 million in 1976, for a 3-year average of $6.7 million, instead of the $11.2 million proposed by Staff.

The record indicates Appalachian's qualified investments for tax credit purposes will increase substantially over the next five years. Moreover, its experience over the last three years indicates a steady growth of investment from a low point in 1974. The Staff method is found to be reasonable and is adopted by the Commission in calculating federal income tax expense.

C. *"Normalization" of Tax Benefits Due to Accelerated Depreciation and Amortization as Tax Deductions and Investment Tax Credits*

In the past Appalachian has used the "flow through" method of financial and ratemaking accounting with regard to income tax benefits attributable to (1) liberalized depreciation, (2) class life asset depreciation range, (3) asset depreciation range repair allowances and (4) investment tax credits.

Appalachian now wants to shift from "flow through" to "normalization" accounting in order to justify higher rates to its West Virginia customers. Appalachian argues that the benefits of "normalization" will outweigh the burdens.

The concepts of "flow through" and "normalization" accounting are understood to be as follows:

(1) "Flow through" accounting is used where the utility elects to use certain statutory tax-saving or tax-deferring provisions for (a) accelerated depreciation or amortization as deductions from gross taxable income, or (b) tax credits, and then the utility calculates Federal income tax expense for ratemaking purposes on the same basis. "Flow through" accounting in test year ratemaking is sometimes

broadly characterized as a method to allow recovery in rates of "actual taxes paid".

(2) "Normalization" accounting is used where (a) the utility employs straight line depreciation for tax purposes in ratemaking, even though it actually uses an accelerated depreciation or amortization for calculating taxes paid to the Internal Revenue Service and where (b) the benefits attributable to the investment tax credit are distributed over the life of the qualified asset, rather than in the year the tax credit is received.

Appalachian urges approval of its partial shift to "normalization", because it sees the resultant increase in cash flow as a means of improving its debt service coverage and ease its outside financing, as well as a means of increasing the amount of internally generated funds needed for construction. Appalachian argues that normalization is a method of accrual accounting which better matches revenues and expenses for services rendered. It would use an accumulated deferred income tax reserve to reflect the excess of normalized Federal income tax over that actually paid to the IRS during the early years of property life and would deduct the reserve from rate base or give an equivalent portion of the rate base a zero rate of return.

The Staff of the Commission presented its initial evidence on the basis of "flow through" and, subsequently modified its position to favor normalization of all tax benefits, except investment tax credit. At a Staff-recommended 9.42% rate of return level, the cost of service using normalization would be $5,215,951 higher than that obtained from a flow-through calculation. We decline to follow either the Staff or the Company's recommendations. We will adhere to a "flow-through" of tax benefits from liberalized depreciation, class life asset depreciation range (ADR) and ADR repair allowances, but we will allow normalization of investment tax credit benefits.

We reject normalization of tax benefits derived from using optional deductions from gross taxable income, because of our inability to fairly predict the tax effects of future elections by the taxpayer. In this very case, Appalachian changed its position and elected *not* to take accelerated amortization on pollution control facilities which were placed in service in 1975, under § 169 of the Internal Revenue Code because it wanted to minimize the payment of a 10% minimum tax on certain tax preference items and to increase its investment tax credit carryforward and increase its taxable income "without any change in the regular taxes payable".

On the other hand, we will permit the Company to "normalize" its investment tax credit benefits for ratemaking purposes in the unique circumstances of this case. Appalachian has elected *not* to use the option available under Section 46(d) of the Internal Revenue Code which allows an investment tax credit for qualified progress expenditures before the property is placed into service. Since we do not allow all Construction Work In Progress (CWIP) in rate base, we would be reluctant to allow normalization of investment tax credit benefits on property not yet placed in service.

Section 46(f) of the Internal Revenue Code provides the general statutory rule that no investment tax credit will be allowed to a public utility, *if a rate regulatory body* (1) reduces the utility-taxpayer's cost of service for ratemaking purposes by reason of any portion of the investment tax credit, or (2) reduces the utility-taxpayer's rate base to which the rate of return is applied for ratemaking purposes by any portion of the investment tax credit. The tax statute limits this general rule in various ways and without timely utility-taxpayer elections to the IRS. Obviously, the intent of this Federal statute is to encroach on the freedom and jurisdiction of State regulatory bodies

in ratemaking so as to aid public utilities to generate internally or to finance funds for construction of public utility facilities.

The West Virginia Public Service Commission need not raise the question under the 9th and 10th Amendment to the Constitution of the United States of whether Federal tax laws can control or impair a State's rights to regulate intrastate utility rates. We need not do so here because we recognize Appalachian's need for additional cash flow to be able to construct substantial additional facilities to continue to render adequate service to the public. The overall intent of the maze of shifting tax laws is that there should be some measure of *fair sharing* of tax benefits between utility taxpayers having growth problems and the ratepayers who also have limited financial means. By permitting Appalachian to adopt normalization of investment tax credit in this case, the Commission can still regulate Appalachian's level of Federal income tax expense used in ratemaking by an averaging technique such as the 5-year average of qualified investment used by the Staff and approved for this case.

We recognize that it is difficult to predict the tax benefits of future elections as to investment tax credits, but since this will be a direct reduction of taxes in each fiscal year it is more susceptible of fair regulation by averaging than would be the Sections 167 and 169 I.R.C. tax benefits by savings or deferral through "normalization" accounting and ratemaking. We must insist, however, that the rate base be reduced by any accumulated deferred reserve resulting from normalization and the deferred credits should be amortized over the life of the public utility property involved.

Following the methods approved above for calculating a test year, pro forma, Federal income tax expense to be used in ratemaking, we find that $4,573,249 is a fair, just and reasonable amount to be included in total cost of service based upon a 9.35% rate of return on a West Virginia rate base of $488,550,995 for the first-tier rates effective August 28, 1975 through April 30, 1976. Furthermore, we find that $4,596,410 is a fair, just and reasonable amount to be included in total cost of service based upon a 9.35% rate of return on a West Virginia rate base of $488,976,907. For the second-tier rates effective on and after May 1, 1976, see Appendices B and C attached hereto.

9. Jurisdictional Cost Apportionment

The second step in the ratemaking process, after determining the aggregate test year, pro forma total cost of service or revenue requirements, is to decide how much of the total is the fair responsibility of West Virginia *vis a vis* Appalachian's other markets in Virginia regulated by the Virginia State Corporation Commission and Appalachian's markets regulated by the Federal Power Commission. We approach this task with caution, not only because the process of jurisdictional cost apportionment is complex and ephemeral, but also because it should not put the customers in any rate jurisdiction or the Company itself at an undue or unreasonable disadvantage. In short, we must be fair and balanced in our determination of this issue.

Before considering subsidiary issues, certain factual data should be set forth as a point of reference that is not lost in a welter of statistical evidence. Upon the premise that the regulatory bodies of West Virginia, Virginia, and

the Federal Power Commission set rates on the basis of costs and each has to apportion total costs for ratemaking purposes in their respective jurisdictions, we note Appalachian's sales volumes, and unit revenues per kilowatt-hour sold over the period 1971 through 1976.

Except for unavailable interchange-out sales revenues to non-affiliates on billing units of 573,872 megawatt-hours in 1971 and 623,347 megawatt-hours in 1976, Appalachian's gross revenues increased from $238,924,000 in 1971 to $677,499,000 in 1976. Dividing pertinent kilowatt-hours sold of 19,552,038,000 in 1971 and 31,853,031,000 in 1976 into these revenues we find Appalachian's *aggregate* unit revenues increased from 1.22¢ per kilowatt hour in 1971, to 2.12¢ per kilowatt-hour in 1976, on said sales volumes. The underlying unit revenues by rate jurisdiction is shown on Appendix D hereto and as follows:

		1971	
1.22¢/Kwh on Aggregate Sales of 19,552,038,000 Kwhs	1.34¢/Kwh on	(W.Va.)	sales of 7,407,817,000 Kwhs
	1.44¢/Kwh on	(Va.)	sales of 6,216,874,000 Kwhs
	.92¢/Kwh on	(FPC)	sales for resale of 3,786,979,000 Kwhs
	.70¢/Kwh on	(FPC)	sales to affiliates of interchange-out of 2,140,368,000 Kwhs
		1976	
2.12¢/Kwh on Aggregate Sales of 31,853,031,000 Kwhs	2.64¢/Kwh on	(W.Va.)	sales of 8,745,946,000 Kwhs
	2.69¢/Kwh on	(Va.)	sales of 7,875,839,000 Kwhs
	1.71¢/Kwh on	(FPC)	sales for resale of 9,159,250,000 Kwhs
	1.30¢/Kwh on	(FPC)	sales to affiliates of interchange-out of 5,961,996,000 Kwhs

A. *Energy Cost Apportionment*

Several observations can be made from the foregoing facts, and Appendix D hereto, which also shows the detail of the intervening years between 1971 and 1976. First, for those who are "marginal cost" or "long run incremental cost" devotees, using 1971 as a base, Appalachian's growth in energy sales is shown to be predominately the responsibility of its FPC jurisdictional customers who purchased 9,243,374,000 Kwhs (or 75.9%) of Appalachian's incremental growth of energy sales 1976 over 1971 of 12,340,468,000 Kwhs. On a comprable [sic] basis, West Virginia realized a growth of 1,338,129,000 Kwhs (or 18.1%) and Virginia experienced an incremental increase in sales of 1,658,965,000 Kwhs (or 26.7%).

Yet, even with the substantial increase in energy requirements of the interstate market, Appalachian increased its unit revenue yield in 1976 over 1971 only by .60 (Interchange-out to affiliates) and .79 (Sales for resale) cent per kilowatt-hour for the FPC jurisdiction, which required the largest growth of energy requirements. In contrast, Appalachian exacted an incremental unit revenue increase of 1.30¢/Kwh for West Virginia and 1.25¢/Kwh for Virginia.

This Commission fully recognizes that the aggregate of sales under FPC jurisdiction may cost less per unit than does the aggregate of sales in the two State jurisdictions. This is because certain of the sales under FPC rate schedules may justify a lower demand cost responsibility than do the State sales and for other reasons, such as that a "wheeling" power service has little or no *energy* cost responsibility. However, the major cost increase experienced by Appalachian during the period 1971 through 1976, has been the hyper-inflationary jump in fuel costs. With this in mind, the substantially lower unit revenue increases for *FPC* jurisdictional sales as compared with *State* jurisdictional sales are suspect. It will only be with a fully

distributed jurisdictional cost apportionment study that regulatory bodies can act to avoid the possibility that West Virginia and Virginia are subsidizing Appalachian's interstate sales.

Both the Staff and Appalachian credited interchange-out revenues to total cost of service prior to the apportionment of costs by segregation or allocation factors based upon demand and energy components. Therefore, we have no way to test whether or not such FPC rates are too low against the backdrop of escalating fuel costs. We do know, however, that the use of the "revenue-credit-to-cost of service" method sponsored by Appalachian would assign cost recovery deficiency in such sales to West Virginia. In view of the lack of evidence on this issue involving interchange-out sales, we can do no more than accept the revenue-credit method used by Appalachian and the Staff for interchange-out sales. However, since the energy growth responsibility is shown to have been that of the FPC jurisdiction, we believe our concession in this regard is in favor of the Company and counterbalances other determinations in this order which Appalachian might consider as less than liberal to the utility.

In Case No. 8401, order issued April 29, 1976, we adverted to these same problems, and those pertaining to the lack of accurate and complete demand data, for use in cost apportionment. We noted there that:

> "Appalachian has embarked on a load research program to determine by sampling a more representative assignment of cost responsibility for its rendition of service."

Although this is more appropriate to cost apportionments to classes of service, rather than to jurisdiction, we are putting Appalachian on notice by this order that we expect Appalachian to come in with a full cost apportionment study *with measured data* as far as possible in its next rate case.

This Commission is charged with the responsibility of protecting West Virginia customers from the burden of any undue or unreasonable subsidization of other markets. We turn now to the issue pertinent to the *demand* responsibilities for assigning costs.

B. *Demand Cost Apportionment*

Unlike energy sales, all of the peak hourly demands (KW) of jurisdictions and classes of service are *not* measured. Those not measured are derived by formula. Nevertheless, the Company attempts to assign *demand* cost responsibility on the basis of peak hour demand, even though there is very little measured data of peak demands. Appalachian (1) uses demand allocation formulas that impute demands to classes of service of jurisdictions or else (2) it credits revenues against production costs before demand or energy allocations are begun. The latter method creates the fiction that such revenues cover a fair portion of all of the costs of such service. In the opinion of this Commission, unless such sales treated by the "revenue credit" method are relatively insignificant, the crediting of such revenues against total costs prior to cost apportionment is tantamount to assuming the fact in issue or "begging the question" of the fairness of cost apportionments within the total. Cf. Case No. 8000, *Columbia Gas of West Virginia, Inc.*, order issued May 14, 1975.

In its evidence, Staff included the measured peak hourly demands of Appalachian's short-term, limited term and unit power sales in megawatts in the development of the Staff's demand related allocation factors. Also, Staff included kilowatt hours of sales from these customer classes in the development of energy related allocation. These sales are regulated by the Federal Power Commission. Appalachian characterizes them as "non-firm" sales, even though they are "firm" to the extend [sic] of their contract

terms and have high priority in the event of future power shortages.

Appalachian opposes the staff approach on this issue, even though it had used the same method in its last major rate case, No. 7083, decided by this Commission. It does so on the ground that since neither Appalachian nor its parent plans or constructs facilities for short term, limited term or unit power sales that these classes of customers are not responsible for a fair portion of the costs of the system installed and operated to render all service.

The record indicates that even if it is true that Appalachian's system is not planned for these sales, there is no question that its system was *used* for these sales on the peak hour and in energy or commodity sales. The Commission finds that costs should be apportioned after considering the percentage effects of the *actual use* of facilities during the test year on the peak hour, as well as throughout the test year. In an integrated electric system having periodic spurts of growth, new capacity is made available prior to the time needed. The members of the system, as well as outside purchasers of power for resale know that there will be excess power available by design or by the principle of diversity, until growth stops at some unknown point in the future. When such customers contract for service, other than (1) purely emergency energy service, (2) interruptible economy energy service or (3) surplus or dump energy service, they pay a rate which includes a capacity or demand charge. If any service has a demand cost element underlying the capacity charge in its rate, that service should be tested to be sure that it bears a *fair* portion of the demand costs. Crediting such revenues against costs by-passes this issue. It would permit the Company to avoid the determination of the question of "How much is fair?".

What should not be lost sight of is the use that is made of a demand allocation factor. For example, staff applies the demand-allocation factor to most transmission operation and maintenance expenses. These expenses are for the benefit of the short-term, limited-term and unit-power customers, as well as other customers of Appalachian. All of these customers should bear a portion of the capacity costs of the facilities used to serve them.

We find that the staff method of jurisdictional cost apportionment is just and reasonable.

10. *Class of Service Cost Apportionment*

The third step in the ratemaking process is to assign the West Virginia costs to the classes of service within West Virginia which are subject to the rate jurisdiction of this Commission. This step is a necessary prelude to the final step or ultimate rate design process in ratemaking.

Classes of service within West Virginia include residential, commercial, industrial and others (sales for resale [FPC], street lighting, and sales to public authorities).

The costs of service for these classes should also involve cost apportionments if there is to be a change in rate design from historical differentials. Even if there is no change in rate design, the Commission should periodically test the propriety of the differences in rates as among classes of service. "Class of service" cost apportionment is just as complex and ephemeral as is "jurisdictional" cost apportionment.

Here, too, those who are "marginal cost" or "long-run incremental cost" devotees tend to jump to the conclusion that industry is responsible for Appalachian's growth and that the residential market is subsidizing the industrial market.

Our point of reference is the growth of sales volumes and revenues by classes of service over the period 1971 through 1976. See Appendix E hereto.

An interesting observation from this factual data is that, using 1971 as a base, the incremental growth of Appalachian's 1976 sales in West Virginia amounting to an aggregate of 1,354,505,189 kilowatt-hours is attributable as follows to the classes of service:

	KWHs	%
Residential	884,396,695	65.7
Commercial	379,778,318	28.0
Industrial	67,570,242	5.0
Others (Sales for resale [FPC], street lighting and sales to public authorities)	22,759,934	1.3
Total	1,354,505,189	100.0

In the face of these growth patterns of energy sales, realization of unit revenues by classes are as follows:

	Cents Per Kilowatt-Hour		1976 Over 1971
	1971	1976	%
Residential	2.09	3.22	54
Commercial	1.91	3.18	66
Industrial	.94	2.10	123
Others (Sales for resale [FPC], street lighting and sales to public authorities)	1.76	2.39	36
Total	1.38	2.63	91

These comparisons show that the *industrial* market grew by only a 5% increment of total market growth, while paying Appalachian a 123% incremental increase in unit revenues. On the other hand, the *residential* market grew by a 65.7% increment of the total growth, while providing Appalachian a 54% incremental increase in unit revenues. This is *not* to say that unit revenue growth by classes of service should match or even closely approximate growth in kilowatt-hours of sales. However, the great disparity shown is indicative that cost apportionment by classes of

service is required to test the fairness of rates as among classes of service in West Virginia. This is particularly true, since the accelerated fuel costs is [sic] such a large part of Appalachian's cost of service.

Neither Appalachian nor the Staff submitted cost apportionment studies by classes of service. In our order issued April 29, 1976, in Case No. 8401, we noted that Appalachian contended it was not possible to allocate peak demand among classes of customers, since only a small part of the component parts of that peak hourly demand among various classes of customers is measured. Appalachian has been put on notice for more than two years, that it must prepare such a study. It is our understanding that such a study by use of a sampling technique is soon due. A fully distributed cost apportionment study by classes of service will be required.

11. *Rate Level and Rate Design*

The final step in the ratemaking process is to set rates, tolls or charges for service to each customer class and for each demand and usage block at rate levels which are no more than the specific service is reasonably worth to the various customers "considering the cost thereof". Code 24-2-2. These rates and charges must be just, reasonable and fair to all segments of the public involved. Code 24-2-3. The public involved includes the public served and the public servant. The public served includes classes of customers, as well as customers within each class that require very little electricity or extremely large amounts of power. These requirements may and often do vary from hour-to-hour, from day-to-day, from month-to-month, from season-to-season and from year-to-year. Since the metering for these peak and volume fluctuations over various periods of time, and the compilations of the resulting measurements would be extensive and expensive, various compromise rate

forms have been designed and used to achieve rate fairness. One of these rate designs is the declining block form of energy rates as a simplification of cost related rates.

Currently, there is a lack of understanding of the declining block rate form leading to debatable conclusions, which, if put into effect, may adversely affect the well-being of every element of the public. There are those in influential positions who say that electric rates should not have a lower tail block rate for the large users. They contend that this is "promotional" and provides high usage customers with an unfair preference over low use customers. Moreover, the argument goes further to characterize declining block rates as being contrary to a conservation of energy policy and a burden on the poor.

The Parable of Milk

Often, both experts and newcomers in the energy-rate debate deal with the pet phrases and esoteric vocabulary of the controversy without a full understanding of the limits and ambivalence of the terms and pertinent concepts. Thus, for a better understanding of declining block rates and their underlying costs, we believe that an explanation by way of analogy in terms of the sale of milk would be helpful.

Our parable involves two extremely poor families—(1) an elderly widow on social security who lives alone, and (2) a husband and wife with two children living on welfare.

The *elderly widow* buys a quart of milk a week at 50 cents a quart, from which she can drink 5 glasses of milk each week at 10 cents per glass. She cannot buy more than a quart of milk a week because she does not have the money. Even if she did have an extra 50 cents, she would not buy a second quart or a half gallon of milk because it might spoil in her tiny refrigerator.

The *welfare husband* buys a gallon of milk a week at $1.50 per gallon, from which he, his wife and their two little

children can drink 20 glasses of milk. Thus, each of the four persons can drink 5 glasses of milk each week at 7½ cents per glass.

Looking at these two sales *from the point of view of the supplier,* it costs the dairy more to supply a quart of milk than it does to supply a gallon. The dairy pays more per carton to buy a few quart cartons, fill them, and handle them, than it does for it to buy the more popular gallon cartons, fill and handle them. The dairy may have less of a profit margin on each six ounces of milk sold by the *quart,* than it does on each six ounces of milk sold by the *gallon.*

Although the analogy is not perfect, these prices could be stated in a "declining block" price form, rather than a "per carton" price form, to be 10 cents per glass for the first 5 glasses of milk and 6.67 cents per glass for the tail block of 15 glasses of milk.

From the point of view of the two poor milk customers, the widow cannot justly complain that she is being discriminated against because her milk purchased by the quart costs her 10 cents per glass rather than 7½ cents per glass when purchased by the gallon. If the welfare husband was forced to pay 10 cents, instead of 7½ cents per glass, such would not encourage conservation of milk.

If government stepped in and ordered the dairy to reduce the price of a quart of milk from 50 cents to 38 cents, so that the widow could get milk at 7½ cents per glass, it is possible that the dairy could not sell milk in quarts at that price without suffering an out-of-pocket loss. It would not be just for the dairy to raise the price of a gallon of milk to the welfare husband, so as to make up for the loss from the sale to the widow at below cost.

Application of the Parable to Electricity

Any arbitrary, blanket condemnation of the declining block form of electric rates can very easily create the same

kind of potential injustice as is suggested in the milk parable. Without valid studies of the cost of supply power at various voltages, demands and amounts of energy, flattening or inverting the block form for electric rates can cause the utility to sell power at a substantial loss or require other customers to pay an inordinate electric rate to subsidize the low user. Although the poor person is more often than not a low user of power this is not always the case. Moreover, there are many more electric customers in West Virginia who are *not* poor and who are also low users of electricity.

In the discouragement of large uses of power by high rates and abruptly changing rate forms, such discouragement does not distinguish between the prevention of *good* uses of electricity and *wasteful* uses. Morover, if the large users of electricity are providing the utility with substantial amounts of revenues to cover the utility's costs and profit margin, any forced reduction in use in substantial amounts by penalty pricing may either cause the utility to shift the cost burden to other customers or absorb the loss itself and thus weaken its financial condition and its ability to serve.

By this discussion this Commission does *not* imply that electric rates should not be flattened or changed in any way from the declining block rate form. We merely caution that it should not be done abruptly or without valid supporting cost apportionment studies.

We turn now to the rate design issues posed for decision in this proceeding.

Residential Rate Design

Appalachian proposes to eliminate its lower water heater service rate for residential (R.S.) customers, and after eliminating or phasing out its Church Service (C.S.), Electric Heating-General (E.H.G.), School Service (S.S.),

Capacity Power (C.P.) and Large Power (L.P.) services, it would spread the rate increase by an across-the-board percentage.

Appalachian Research and Defense Fund, Inc., et al, ("Low Income Intervenors") urge the Commission to grant little or no increase in the residential rate, and an increase of .21¢ per Kwh for the commercial and industrial customers who purchase under the Commercial-Industrial Power (C.I.P.), Large Capacity Power (L.C.P.), Transmission Power (T.P.) and High Load Factor Power (H.L.P.). The Low Income Intervenors urge a departure from the declining block rate structure to an inverted block rate structure of 2¢ per Kwh for all usage above 200 Kwh and 4¢ per Kwh for all usage above 200 Kwh per month, *but* with *credits* given for off-peak usage for electric hot water and/or electric space heating. In addition, they recommend "the reduction of 'submarginal' rates", which is interpreted by the Commission to mean that any rate preference now being given to the low use or initial block rates should be further reduced. The theory underlying this proposed rate innovation and attack on the declining block rate form is that of "marginal cost" or "long run incremental cost". As to "peak load" or "time of day" pricing, the Low Income Intervenors do *not* recommend that residential customers be put on that type of metering or rate form at the present time, because the cost of necessary metering would be too high.

Protestant, Council of Senior Citizens, contends that Appalachian's tail blocks are too low and *assumes* that the growth in demand causing Appalachian to grow in demand and energy supply is due to the requirements of the industrial and commercial markets.

FMC Corporation, ACF Industries, Inc., American National Rubber Co., Chemetron Corporation, Huntington Alloys, Inc., Houdaille Industries, Inc., and Owens-Illinois,

Inc., ("Industrial Intervenors") oppose the "marginal cost" theories and rate design proposals of the Low Income Intervenors. They point to the danger of loss of industry to other States by excessive rates to West Virginia industry. They discuss weaknesses in the theory and factual background of the "marginal cost" arguments made by the Low Income Intervenors.

The Staff of the Commission notes that the record is bare of a fully distributed cost of service study by customer class, but that such a study (requested by the Commission in April of 1975) was expected soon. In this posture, the Staff opposes the elimination of certain rate schedules and would spread any revenue deficiency over all classes of service on a percentage basis.

The Commission finds that in the absence of a cost apportionment study or studies, it will generally adhere to the historical rate form, with certain minor discretionary modifications, and will deny the proposed changes in rate form made by Appalachian and urged by the Low Income Intervenors. We do this without prejudice to our future actions which may change the historical rate forms used by Appalachian on the basis of valid cost apportionments and other considerations.

On the present record we have no way of knowing whether the discount given to residential water heating customers or electric heating-general customers is fair or not. It could very well be that a cost apportionment study would indicate that the large users in the residential class of service are already contributing more through the low blocks of their rates towards the costs of serving them than is justified. The opposite could also be true.

We do know, however, that the residential market in West Virginia is more responsible for Appalachian's growth over the period 1971-1976 than is the industrial market, although it appears that the major cause of growth

is due to the demands for electricity outside of West Virginia. Thus, if we were to be influenced by the "marginal cost" or "long run incremental cost" theorists, we would be led to the conclusion that the residential market growth is more responsible for Appalachian's growth of facilities in a hyper-inflationary age, than is industry.

As to the Low Income Intervenors' recommendation that the block rate form be inverted, not only is the record void of probative evidence to quantify such a rate form on a just, reasonable and fair basis among the various classes of customers—even with a preferential bias to the residential class, but also the argument of the Low Income Intervenors is weakened by their recommendation of a *credit* (of unknown magnitude) for water and space heating customers.

We do recognize that the debate is not ended and that the poor customers do have a need for every consideration. Therefore, in an effort to move towards a gradual flattening of the declining block rate form, we will design residential rates herein which will spread the rate increase *after skipping the first usage block* of the R.S. rate schedule. We do not do this arbitrarily, but act after analysis of the effect of Appalachian's informational filing pursuant to ordering Paragraph 4 of our order issued January 31, 1975, in Case No. 7083, and the facts of record in this case.

The "end results" of this and other rate design issues determined herein are set forth in Appendix F to this order.

Abrupt Elimination of Industrial and Commercial Rate Schedules

In Appalachian's proposed W.Va. P.S.C. Tariff No. 3, in effect tentatively since August 28, 1975, in addition to its abrupt elimination of the water heater service for residential customers discussed above and reinstated herein, Appalachian deleted its Combined Light & Power (C.L.P.), Capacity Power (C.P.), and Large Power (L.P.) rate schedules previously available to certain of its industrial and commercial customers.

The Commission has been informed that Appalachian had no commercial customers purchasing under its C.L.P. rate schedule. We have no objection and approve the deletion of this portion of the tariff as superfluous. The C.P. and L.P. rate schedules were previously available to certain customers. We find that Appalachian failed in its burden of proof to justify the deletion of these services, because it presented no cost data to support its managerial decision and other considerations discussed below.

L.P. Rate Schedule

The Large Power service rate was available to customers who contracted to pay for a definite, large amount of electrical capacity in excess of 50 KVA in multiples of 25 KVA. The rate was composed of a demand charge and a declining block energy charge, with a minimum monthly charge also composed of demand and energy components. The record does not reflect which customers were served under this rate schedule. After the L.P. schedule was abruptly eliminated, it is thought that such customers would begin purchases under the Commercial-Industrial Power (C.I.P.) schedule. The C.I.P. schedule had the same demand energy form and level of rates as did the L.P. schedule. However, the minimum charges of the C.I.P. schedule was higher than that in the L.P. schedule and would cause customers affected to experience a higher per unit cost of electricity under the C.I.P. schedule if the load factor of purchases fell below a certain level. Those coal mines which purchased power under the L.P. schedule would be adversely affected by its deletion if they were relatively low load factor customers. We cannot eliminate the L.P. schedule on the basis of the record before us.

C.P. Rate Schedule

Appalachian proposes the deletion of the Capacity Power rate schedule available to industrial power users (other than coal mines). The C.P. schedule is a primary-secondary type rate, with two sets of declining block rates keyed to use and to the customers' contracts for electric capacity in amounts over 50 KVA and in multiples of 25 KVA. The C.P. rate was apparently designed for the low load factor industrial customer.

The elimination of the C.P. schedule on and after August 28, 1975, forced the C.P. customers to elect between the General Service (G.S.) and the Commercial-Industrial Power (C.I.P.) rate schedules.

The impact of Appalachian's filing is illustrated by the plight of the letter-Protestant, Guyan Machinery Co. ("Guyan") of Logan, West Virginia. Guyan protests that they were forced to purchase under the C.I.P. schedule after August 28, 1975, because Appalachian's G.S. schedule was "plain murder" and Guyan's low use made unavailable the other Appalachian schedules granted coal mines and other large volume users. Guyan complained that being forced to go to the C.I.P. schedule gave them a "double" increase, that is, (1) an increase resulting from going from the more-favorable C.P. to the C.I.P. schedule, plus (2) the rate increase proposed for the C.I.P. schedule.

The creation of several classes of service depends upon a combination of distinctive load characteristics (magnitude of demand, load factor, time of use, frequency and duration), as well as special physical circumstances of large industrial demands and purchases in relation to the utility's facilities and capacity. The nature of the customer's functions or its societal context as an industry, commercial business, school, church or other institution is also important in justifying *reasonable* rate differentials and separate rate forms.

As a general rule the Commission favors a reduction in the number of rate schedules in a tariff in order to simplify the administration, regulation and understanding of customer billings. However, we do not approve the deletion of rate schedules, which certain customers have come to rely upon, without something more tangible and persuading than the mere simplification of a tariff.

We must have more than a mere assertion that certain rate forms were "promotional" and are deleted because they were "designed years ago to serve coal mining customers and which cannot be justified on a cost of service basis in today's economic climate". The record does not support this assertion. We suggested in Case No. 7083 by our order issued January 31, 1975, rate changes should not be abrupt in departing from historical rates because customers in various classes of service have geared themselves to rates and rate forms in effect. An abrupt change would destroy this relationship without good cause and do violence to the maintenance of good faith between the utility and its customers.

We will require that the C.P. and L.P. rate schedules be reinstituted and that the respective C.P. and L.P. customers who purchased under these rate schedules when they were last effective will have the option of choosing to be billed thereunder at the higher rates allowed herein for the period after August 28, 1975, and to receive refunds accordingly.

Gradual Elimination of Certain Services

Appalachian proposes to gradually eliminate its Church Service (C.S.), School Service (S.S.) and Electric Heating-General (E.H.G.). It would phase out these rates over a 4-year period by imposing a cumulative 10% surcharge each twelve months for the period ending August 27, 1979. At some point before the end of the 4-year period Appalachian would anticipate that its customers, severally, would find it economically advantageous to shift to the G.S., C.I.P. or P.S.O. (Public School Optional) schedules.

Here, too, no cost apportionment by classes was presented on the evidentiary record. The schools, churches and general service (non-residential) heating customers have been paying higher declining block rates, plus a 10% surcharge in 1975-1976 and a 20% surcharge in 1976-1977. The Commission is informed that certain of these customers, including the churches, have had demand meters installed by Appalachian.

Protestant, Kanawha Valley Baptist Association, through its moderator, Mrs. Lucille E. Gillispie, presented evidence and argued persuasively that the elimination of the C.S. schedule was demonstrably unjust. The Staff of the Commission agrees and noted Mrs. Gillispie's testimony that the "concept of the demand meter is prejudicial against churches which have activities primarily on one day, and that day being when industry is at its lowest ebb".

We find that the churches and schools are distinctive institutions dissimilar in character from the residential, commercial and industrial institutions in several ways that have relevance to utility service and pricing with reference to load characteristics, economics, philosophy of pricing, and societal context.

We find that E.H.G. service, as well as C.S. and S.S. service cannot be eliminated, even gradually, without a consideration of the cost of such service in relation to what each is reasonably worth.

Appalachian will be required to reinstate the C.S., S.S. and E.H.G. rate schedules without the surcharge and at the lower block rates determined in this order and refund to the respective customers the entire surcharges collected, plus the difference in the filed block rates and the lower approved block rates. Our action here has support in principle under *Clarksburg Light and Heat Co.* v *P.S.C. of W. Va.*, 84 W.Va. 638, 100 SE 551 (1919); *Anchor Coal Co. et al* v *P.S.C. of* W. Va. [sic], 123 W. Va. 439, 15SE 2d 406 (1941).

Other Tariff Provisions

Appalachian also filed two new schedules, R.E. (Rural Line Extension Plan) and T.S. (Temporary Service). In Staff's brief we are urged to approve for West Virginia, the wording of Appalachian's Virginia tariff relating to extension of service as being more specific. Staff also urges that "residential customers" should be excluded from certain limitations in the tariff provisions related to "Service Connections" and "Use of Energy By Customer", which are sections in tariff's "Terms and Conditions of Service". Finally, Staff urges that residential customers who have their service discontinued, should be excused thereafter from paying any minimum bill. These suggested changes do not appear to be opposed by Appalachian or the other parties to the proceeding and are approved. They are in the public interest and some will be further modified so that Appalachian's tariff will be in conformance with our recently promulgated Rules and Regulations for the Government of Electric Utilities.

Although not raised in any of the briefs, we note that Appalachian has changed the form of its minimum monthly charge for its L.C.P. service. The record is void of any support for this change in rate design. Appalachian will be required to revert to the *form* of minimum charges contained in its tariff sheets in effect April 1, 1975 through August 27, 1975, without prejudice to changing its minimum charges in future rate proceedings upon a consideration of costs and other pertinent factors.

The specific tariff provisions discussed and required to be modified are set forth in Appendix G hereto.

FINDINGS

In addition to the decisional findings and conclusions above, the Commission finds as follows:

1. The rates and charges set forth in Appalachian Power Company's Tariff W.Va. P.S.C. No. 3 issued March 31, 1975,

and put into effect August 28, 1975, by terms of West Virginia Code, Chapter 24, Article 2, Section 4, are unjust and unreasonable for the reason that they would produce more revenues than are necessary to enable Appalachian Power Company to pay its reasonable and necessary operating expenses, taxes, and depreciation, and earn a fair return on its property used and useful in its public service business in the State.

2. Appalachian Power Company did not sustain its burden of proof to avoid undue rate discrimination under West Virginia Code, Chapter 24, Article 2, Section 2, so as to justify its proposed modifications in the rate forms contained in the R.S., L.C.P., C.S., E.H.G. and S.S. schedules and its proposed deletions of the C.P. and L.P. schedules as of and after August 28, 1975.

3. The changes proposed by Appalachian Power Company in the "Terms and Conditions of Service" portion of its filed tariff on Original Sheet Nos. 3-1, 3-2, 3-3, 3-4 and 3-5, are not supported by the evidence and are not in the public interest to the extent that they may substantially depart from Part 4.00 Customer Relations of the Rules and Regulations for the Government of Electric Utilities promulgated by this Commission as of March 1, 1977, and soon to be in effect in May 1977 and thereafter, unless modified.

4. The rates, charges and tariff provisions hereinafter approved, are just, reasonable and not unduly discriminatory.

Order

1. The tariff sheets filed with the Commission by the respondent, in its Tariff W.Va. P.S.C. No. 3, issued March 31, 1975, are hereby cancelled and stricken from the tariff files of the Commission, except for Original Sheet Nos. 2-1, 2-2, 2-3, 2-4, 2-5, 12-1, 12-2 and 13.

2. The rates, charges and tariff provisions set out in Appendix F, Columns IV and V and Appendix G attached to this order are approved, severally, to become effective on and after August 28, 1975 and May 1, 1976, as shown or required therein.

3. Appalachian is ordered to utilize the *form* of minimum monthly charges as is contained in its tariff sheets approved by our Order issued August 9, 1976 in Case No. 7083, in the schedules to be filed.

4. Appalachian is ordered to file revised tariff sheets to supersede those sheets requiring modifications for its W.Va. P.S.C. Tariff No. 3, within fifteen (15) days of the date of this order for approval by this Commission as to their conformity with the findings and conclusions stated herein.

5. Appalachian shall refund to each of its customers entitled thereto, within sixty (60) days of the date of this order the amount of excess collected under the rates placed into effect under bond and the amount which would have been collected under the rates that are herein approved, with interest thereon, at the rate of seven and three-quarters per cent (7¾%) per annum, until paid; that refunds of Five Dollars ($5.00) or less may be made by crediting the amount of the subscriber's account, and that as to amounts in excess of Five Dollars ($5.00) the refund shall be made by check.

The respondent shall report to the Commission the amount refunded, including the interest, the manner of refunding and the amount, if any, which it has been unable to refund.

6. Appalachian shall rebill each customer, who had been billed under the C.P., L.P., C.S., S.S., or E.H.G. schedules prior to August 28, 1975 for the two periods which began

August 28, 1975 and May 1, 1976, so as to give the customer the option of requesting and receiving refunds under the prior rate form or the schedule under which the customer actually purchased power during the two refund periods.

7. Appalachian is hereby ordered to file in any of its future rate adjustment filings for service to West Virginia's retail customers, as part of its Tariff Rule 42 data, at least two cost apportionment studies, which will set forth fully-distributed cost responsibilities to West Virginia, Virginia and the Federal Power Commission jurisdictions and as to Appalachian's various classes of service; one study shall be on either a coincidental or non-coincidental peak basis and the other study shall be on the Excess Demand method.

A Copy.

Teste:

s/ S. Grover Smith, Jr.
S. Grover Smith, Jr.,
Secretary

APPENDIX A (CASE NO. 8182)

APPALACHIAN POWER COMPANY

BALANCE SHEET—YEAR END RATE BASE AND CAPITALIZATION AT 12/31/74

	Balance Sheet at December 31, 1974 (In Thousands)		Appalachian Rate Base Calculation December 31, 1974 (In Thousands)		Appalachian Capitalization at December 31, 1974 (In Thousands)	
ASSETS AND OTHER DEBITS						
Utility Plant	1,475,026		1,475,026			
Construction Work in Progress	104,201		104,201			
Total Utility Plant	1,579,227		1,579,227			
Accumulated Provision for Depreciation	(355,740)		(355,740)			
Net Plant		1,223,487	1,223,487			
Other Property		75,170				
Current Assets		176,423	68,556	Prepayments, Materials & Supplies		
Deferred Debits		47,232				
Total Assets and Other Debits		1,522,312				
LIABILITIES AND OTHER CREDITS						
First Mortgage Bonds	669,748				669,748	Long-Term Debt
Debt Premiums	1,936	671,684				
Sinking Fund Debentures	40,153				40,153	Sinking Fund Debentures
Debt Premiums	229					
Sinking Fund Requirement	(468)	39,914				
Installment Purchases		24,000			24,000	Installment Purchase Contracts
Total Long-Term Debt		735,598				
Preferred Stock		109,799			109,799	Preferred Stock
Common Stock		117,958			117,958	Common Equity
Other Paid-In Capital		159,168			159,168	Common Equity
Retained Earnings		110,899			110,899	Common Equity
Current Liabilities		244,373			126,090	Short-Term Debt
Deferred Credits		44,517	(7,803)	Deferred Federal Income Tax-Liberalized Dep.	19,048	Deferred Fed. Inc. Tax —Accelerated Amortization
Total Liabilities and Other Credits		1,522,312				
			33,779	*Working Cash Allowance	20,588	Common Equity—Subsidiary Earnings
			1,318,019	Total Rate Base	1,397,451	Total Capital

* Calculated

APPENDIX B (CASE NO. 8182)

APPALACHIAN POWER COMPANY

COST OF SERVICE COMPONENTS AND REVENUE DEFICIENCY PER COMMISSION ORDER
TEST YEAR 1974
WEST VIRGINIA OPERATIONS
FIRST TIER

A. COST OF SERVICE COMPONENTS

	Operating Revenues	Operating Expenses	Depreciation and Amortization	Taxes—Other Than Federal Income Tax	Average Rate Base
	$	$	$	$	$
Per Staff Exhibit No. 8	176,075,074	105,990,991	17,334,859	16,023,424	488,448,552
Adjustments:					
Coal Expense @ 1.00 per MBTU		120,512			
April, 1975 Wage Increase		779,515			
Payroll Tax Adjustment				46,592	
Working Cash Adjustment Resulting From Operating Expense Adjustments					102,443
As Adjusted	176,075,074	106,891,018	17,334,859	16,070,016	488,550,995

B. COST OF SERVICE AND REVENUE DEFICIENCY

Allowance for Return @ 9.35%	$ 45,679,518
Operation and Maintenance Expenses	106,891,018
Depreciation and Amortization	17,334,859
Federal Income Tax	4,573,249*
Other Taxes—Before Additional Business and Occupation Tax	16,070,016
Additional Business and Occupation Tax	916,663*
Total Cost of Service	$191,465,323
Revenue Deficiency	$ 15,380,249

NOTE: * Calculated After Other Adjustments.

APPENDIX C (CASE NO. 8182)

APPALACHIAN POWER COMPANY

Cost of Service Components and Revenue Deficiency Per Commission Order

Test Year 1974

West Virginia Operations

Second Tier

A. COST OF SERVICE COMPONENTS

	Operating Revenues	Operating Expenses	Depreciation and Amortization	Taxes Other Than Federal Income Tax	Average Rate Base
	$	$	$	$	$
As Adjusted for Period from August 28, 1975 through April 30, 1976 ..	176,075,074	106,891,018	17,334,859	16,070,016	488,550,995
Adjustments:					
Coal Expense @ 1.04¢ per BTU		3,042,433			
April, 1976 Wage Adjustment		1,147,678			
Insurance and Postage Adjustment		236,755			
Increase in F.I.C.A. Base				77,396	
Payroll Taxes on April Wage Adjustment..				68,597	
Working Cash Adjustment					425,912
As Adjusted	176,075,074	111,317,884	17,334,859	16,216,009	488,976,907

B. COST OF SERVICE AND REVENUE DEFICIENCY

Allowance for Return @ 9.25%	$ 45,719,341
Operation and Maintenance Expenses	111,317,884
Depreciation and Amortization	17,334,859
Federal Income Tax	4,596,410*
Other Taxes—Before Additional Business & Occupation Tax	16,216,009
Additional Business and Occupation Tax	1,210,470*
Total Cost of Service	$196,394,973
Revenue Deficiency	$ 20,309,899

* Calculated after other adjustments.

APPENDIX D

APPALACHIAN POWER COMPANY

CASE No. 8182

COMPARISON OF JURISDICTIONAL DELIVERIES AND UNIT REVENUES

1971-1976

	West Virginia			Virginia			Federal Power Commission Jurisdiction										
							Account 447—Sales For Resale			Interchange-Out To Affiliates			Interchange-Out Non-Affiliates		Total	Receipts/ Kwh*	
	Volume	Revenue	Revenue/ Kwh	Volume	Revenue	Revenue/ Kwh	Volume	Revenue	Revenue/ Kwh	Volume	Receipts	Receipts/ Kwh	Volume	Receipts	Volume		
	Mwh	(000) $	% ¢	Mwh	(000) $	% ¢	Mwh	(000) $	% ¢	Mwh	(000) $	% ¢	Mwh	(000) $		% ¢	
1971	7,407,817	99,554	1.34	6,216,874	89,532	1.44	3,786,979	34,785	.92	2,140,368	15,053	.70	573,872	Not Available	6,501,219	.8	
1972	7,661,245	109,044	1.42	6,512,655	98,818	1.52	4,793,612	44,927	.94	6,974,529	39,828	.57	505,914	Not Available	12,274,055	.7	
% Increase — 1971	3.4	9.5	6.0	4.8	10.4	5.6	26.6	29.2	2.2	225.9	164.6	(18.6)	(12.0)		88.8	(14.3)	
1973	8,043,103	118,586	1.47	7,091,705	109,523	1.54	5,681,406	52,169	.92	8,835,857	52,473	.59	587,121	Not Available	15,104,384	.7	
% Increase — 1971	8.6	19.1	9.7	14.1	22.3	6.9	50.0	50.0	0.0	312.8	248.6	(15.7)	2.3		132.3	(14.3)	
1974	8,225,366	169,106	2.06	7,244,332	156,902	2.17	5,704,296	86,203	1.51	7,902,412	97,272	1.23	710,300	Not Available	14,317,008	1.3	
% Increase — 1971	11.0	69.9	53.7	16.5	75.2	50.7	50.6	147.8	64.1	269.2	546.2	75.7	23.8		120.2	60.7	
1975	8,175,885	203,248	2.48	7,356,712	184,022	2.50	6,824,645	113,642	1.67	6,654,970	78,908	1.19	606,466	Not Available	14,086,081	1.4	
% Increase — 1971	10.4	104.2	85.1	18.3	105.5	73.6	80.2	226.7	81.5	210.9	424.2	70.0	5.7		116.7	70.2	
1976	8,745,946	230,789	2.64	7,875,839	212,007	2.69	9,159,250	156,897	1.71	5,961,996	77,806	1.30	623,347	Not Available	15,744,593	1.5	
% Increase — 1971	18.1	131.8	97.0	26.7	136.8	86.8	141.9	351.0	85.9	178.6	416.9	85.7	8.6		142.2	84.5	

NOTE: *Average of Credits to Account 447 and Interchange-Out to Affiliates

Recapitulation of FPC Jurisdictional Energy Sales

	1971	1976	Incremental Growth
	Mwh	Mwh	Mwh
Sales for Resale	3,786,979	9,159,250	5,372,271
Interchange-Out			
—Affiliates	2,140,368	5,961,996	3,821,628
—Non-Affiliates	573,872	623,347	49,475
	6,501,219	15,744,593	9,243,374

Recapitulation of Total Energy Sales

	1971	1976	Incremental Growth	Percent
	Mwh	Mwh	Mwh	%
West Virginia	7,407,817	8,745,946	1,338,129	18.1
Virginia	6,216,874	7,875,839	1,658,965	26.7
Federal Power Commission	6,501,219	15,744,593	9,243,374	75.9
	20,125,910	32,366,378	12,240,468	100.0

APPENDIX E

APPALACHIAN POWER COMPANY

ENERGY—KWH—WEST VIRGINIA

Year	Residential	Incremental % From 1971	Commercial	Incremental % From 1971	Industrial	Incremental % From 1971	Other*	Incremental % From 1971	Total	Incremental % From 1971
1971 ...	1,758,171,438	—	1,180,762,191	—	4,444,695,756	—	95,238,512	—	7,478,867,897	—
1972 ...	1,897,943,511	7.9	1,277,480,451	8.2	4,460,818,707	0.3	100,160,011	5.1	7,736,402,680	3.4
1973 ...	2,119,631,626	20.6	1,388,133,247	17.6	4,509,108,839	1.5	99,153,320	4.1	8,116,027,032	8.5
1974 ...	2,759,265,580	28.5	1,376,687,421	16.6	4,562,796,849	2.7	101,332,651	6.4	8,300,082,501	11.0
1975 ...	2,412,918,831	37.2	1,462,180,687	23.9	4,271,990,226	(3.9)	109,855,026	15.3	8,256,944,770	10.4
1976 ...	2,642,568,133	50.3	1,560,540,509	32.2	4,512,265,998	1.5	117,998,446	23.8	8,833,373,086	18.1

NOTE: * Includes Public Street Lighting, Other Sales to Public Authorities and Sales for Resale.

APPENDIX E—(Continued)

APPALACHIAN POWER COMPANY

REVENUE—$—WEST VIRGINIA

Year	Residential	Incremental % From 1971	Commercial	Incremental % From 1971	Industrial	Incremental % From 1971	Other*	Incremental % From 1971	Total	Incremental % From 1971
1971	36,720,127	—	22,579,790	—	42,000,677	—	1,672,022	—	102,972,616	—
1972	42,746,386	16.4	26,230,008	16.2	47,643,707	13.4	1,793,579	7.2	118,413,680	15.1
1973	47,391,095	29.1	28,709,876	27.2	50,479,767	20.2	1,951,371	16.7	128,532,109	24.9
1974	63,681,382	73.4	36,892,668	63.4	77,588,301	84.7	2,455,118	46.8	180,617,469	75.5
1975	77,669,551	111.5	45,520,195	101.7	92,740,903	120.8	2,804,675	67.7	218,735,324**	112.5
1976	85,071,837	131.6	49,558,673	119.5	94,893,789	125.9	2,821,471	68.7	232,345,770	125.7

NOTE: * Includes Public Street Lighting, Other Sales to Public Authorities and Sales for Resale.

** Includes 7,041,808 Estimated Overrecovery of Fuel Component.

APPENDIX F

APPALACHIAN POWER COMPANY

Comparison of Rates

	I	II	III	IV	V
				Final Commission Approved Rates—Case No. 8182	
	Rates filed pursuant to order dated 8/9/76 in Case No. 7083. Reopened Effective 4/1/75-8/27/75	Lawful Base Rates as of 8/27/75*	Net Rates filed in Case No. 8182**	Effective 8/28/75 through 4/30/76	Effective on and after 5/1/76
	¢/Kwh	¢/Kwh	¢/Kwh	¢/Kwh	¢/Kwh
Tariff C.L.P. (Combined Light & Power) Primary (50 x Capacity) Secondary (Excess over Primary)	Since no customers were being served under this rate schedule it was not submitted by the company.		Discontinued	Discontinued	
First 5,000 Kwhrs					
Next 5,000 Kwhrs					
Over 10,000					
Minimum Charge					
Tariff R.S. (Residential Service)					
First 30 Kwhrs per month	6.169	5.918	6.92426	5.918	5.918
Next 40	5.156	4.905	6.01326	5.338	5.476
Next 130	3.535	3.284	4.07626	3.574	3.666
Next 300	2.623	2.372	2.93726	2.581	2.648
Next 1,000	2.319	2.068	2.48126	2.251	2.309
Over 1,500	2.116	1.865	2.25326	2.030	2.082
Minimum	$ 1.50	$ 1.50	$ 2.50	$ 2.50	$ 2.50
Water Heater Service					
Last 400 Kwhrs per month	2.116	1.865	2.25326	2.030	2.082
Tariff G.S. (General Service) 50 x Monthly Demand					
First 30 Kwhrs	6.169	5.918	7.31226	6.456	6.630
Over 30	4.903	4.652	5.73926	5.078	5.217
Next 150 x Monthly Demand					
First 3,000 Kwhrs	3.535	3.284	4.03126	3.590	3.689
Over 3,000	2.623	2.372	2.90326	2.597	2.671
Over 200 x Monthly Demand	2.116	1.865	2.26526	2.046	2.105
Minimum Charge	$ 1.50	$ 1.50	$ 2.50	$ 2.50	$ 2.50

Notes:

* Not filed because of coincidental effectiveness of proposed No. 8182 rates.

** Filed rates adjusted for credit of .25074¢/Kwh.

APPALACHIAN POWER COMPANY

Comparison of Rates

	I	II	III	IV	V
				Final Commission Approved Rates—Case No. 8182	
	Rates filed pursuant to order dated 8/9/76 in Case No. 7083. Reopened Effective 4/1/75-8/27/75	Lawful Base Rates as of 8/27/75*	Net Rates filed in Case No. 8182**	Effective 8/28/75 through 4/30/76	Effective on and after 5/1/76
	¢/KWH	¢/KWH	¢/KWH	¢/KWH	¢/KWH
Tariff C.I.P. (Commercial-Industrial) formerly C.P.O. (Capacity Power-Optional)					
First 30 x Monthly Demand	5.566	5.315	6.56026	5.800	5.957
Next 170 x Monthly Demand:					
First 3,000 Kwhrs	3.266	3.015	3.70026	3.297	3.389
Next 3,000	3.064	2.813	3.44926	3.077	3.164
Next 4,000	2.861	2.610	3.19926	2.856	2.937
Next 10,000	2.658	2.407	2.93726	2.636	2.711
Next 80,000	2.456	2.205	2.68626	2.416	2.485
Over 100,000	2.253	2.002	2.43626	2.195	2.258
Next 160 x Monthly Demand	1.858	1.607	1.94626	1.765	1.817
Over 360 x Monthly Demand	1.655	1.404	1.69526	1.544	1.591
Minimum Charge	$ 2.00/KVA	$ 2.00/KVA	$ 2.00/KVA	$ 2.00/KVA	$ 2.00/KVA
Tariff P.S.O. (Public School-Optional)					
All Energy	3.636	3.385	4.14926	3.700	3.803
Minimum Charge	$ 2.50	$ 2.50	$ 2.50	$ 2.50	$ 2.50
Tariff E.H.G. (Electric Heating General)					
First 200 Kwhrs	4.143	3.892	4.78826	4.281	4.368
Next 6,800	2.623	2.372	2.90326	2.597	2.671
Over 7,000	2.319	2.068	2.51526	2.267	2.332
Each Kw Demand in Excess of 30	$ 1.27	$ 1.27	$ 1.57	$ 1.38	$ 1.42
Minimum Charge	$ 8.29	$ 7.78	$10.08	$ 8.56	$ 8.74
Tariff S.S. (School Service)					
First 500 Kwhrs per Classroom	3.636	3.385	4.19026	3.700	3.803
Balance	1.812	1.561	1.91126	1.715	1.766
Minimum Charge	$ 2.50	$ 2.50	$ 2.50	$ 2.50	$ 2.50

Notes:

* Not filed because of coincidental effectiveness of proposed No. 8182 rates.

** Filed rates adjusted for credit of .25074¢/Kwh.

APPENDIX F—(Continued)

APPALACHIAN POWER COMPANY

COMPARISON OF RATES

	I	II	III	IV Final Commission Approved Rates—Case No. 8182	V Final Commission Approved Rates—Case No. 8182
	Rates filed pursuant to order dated 8/9/76 in Case No. 7083. Reopened Effective 4/1/75-8/27/75	Lawful Base rates as of 8/27/75*	Net Rates filed in Case No. 8182**	Effective 8/28/75 through 4/30/76	Effective on and after 5/1/76
	¢/KWH	¢/KWH	¢/KWH	¢/KWH	¢/KWH
Tariff C.S. (Church Service)					
First 40 KWHrs per month	6.169	5.918	7.31226	6.456	6.630
Next 85	5.156	4.905	6.04726	5.354	5.499
Next 375	3.839	3.588	4.40626	3.921	4.029
Next 500	2.927	2.676	3.27926	2.928	3.011
Over 1,000	2.623	2.372	2.90326	2.597	2.671
Minimum Charge	$ 1.50	$ 1.50	$ 2.50	$ 2.50	$ 2.50
Tariff C.P. (Capacity Power—Wholesale)			Discontinued		
100 x Contract Capacity:			"	4.411	4.533
100 x First 50 Kva	4.290	4.039	"	3.969	4.079
100 x Next 50 Kva	3.884	3.633	"	2.867	2.948
100 x Next 50 Kva	2.871	2.620	"	2.647	2.723
100 x Next 150 Kva	2.669	2.418	"	2.426	2.496
100 x Over 300 Kva	2.466	2.215	"		
Excess of 100 x Capacity:			"	2.415	2.485
First 50,000 KWHrs	2.456	2.205	"	2.304	2.371
Next 50,000	2.354	2.103	"	2.194	2.258
Next 200,000	2.253	2.002	"	2.140	2.203
Over 300,000	2.203	1.952	"	$25.95/KVA	$26.80/KVA
Minimum Charge	$24.00/KVA	$24.00/KVA			

NOTES:

* Not filed because of coincidental effectiveness of proposed No. 8182 rates.

** Filed rates adjusted for credit of .25074¢/KWH.

APPALACHIAN POWER COMPANY
Comparison of Rates

	I	II	III	IV	V
				Final Commission Approved Rates—Case No. 8182	
	Rates filed pursuant to order dated 8/9/76 in Case No. 7083. Reopened Effective 4/1/75-8/27/75	Lawful Base Rates as of 8/27/75*	Net Rates filed in Case No. 8182**	Effective 8/28/75 through 4/30/76	Effective on and after 5/1/76
	¢/Kwh	¢/Kwh	¢/Kwh	¢/Kwh	¢/Kwh
Tariff T.P. (Transmission Power) For 34.5-69 KV Delivery Voltage					
First 25,000 KVA Demand	$ 6.076	$ 5.324	$ 6.46478	$ 5.793	$ 5.943
Over 25,000 KVA Demand	$ 5.832	$ 5.080	$ 6.15678	$ 5.528	$ 5.671
For 138 KV Delivery Voltage					
First 25,000 KVA Demand	$ 5.934	$ 5.182	$ 6.28178	$ 5.639	$ 5.785
Over 25,000 KVA Demand	$ 5.782	$ 5.030	$ 6.09978	$ 5.473	$ 5.615
Secondary—All Voltage					
Energy in Excess of 300 Kwhrs per KVA Demand	$ 0.01448	$ 0.01197	$ 0.0143326	$ 0.01318	$ 0.01360

Notes:

* Not filed because of coincidental effectiveness of proposed No. 8182 rates.

** Filed rates adjusted for credit of .25074¢/Kwh.

APPALACHIAN POWER COMPANY

Comparison of Rates

	I	II	III	IV	V
				Final Commission Approved Rates—Case No. 8182	
	Rates filed pursuant to order dated 8/9/76 in Case No. 7083. Reopened Effective 4/1/75-8/27/75	Lawful Base Rates as of 8/27/75*	Net Rates Filed in Case No. 8182**	Effective 8/28/75 through 4/30/76	Effective on and after 5/1/76
	¢/KWH	¢/KWH	¢/KWH	¢/KWH	¢/KWH
Tariff L.P. (Large Power)					
First 30 x Monthly Demand	5.566	5.315	Discontinued	5.7994	5.957
Next 170 x Monthly Demand:					
First 3,000 Kwhrs	3.266	3.015	"	3.297	3.389
Next 3,000	3.064	2.813	"	3.077	3.164
Next 4,000	2.861	2.610	"	2.856	2.937
Next 10,000	2.658	2.407	"	2.635	2.710
Next 80,000	2.456	2.205	"	2.415	2.485
Over 100,000	2.253	2.002	"	2.194	2.258
Next 160 x Monthly Demand	1.858	1.607	"	1.765	1.817
Over 360 x Monthly Demand	1.655	1.404	"	1.544	1.591
Minimum Charge	$ 1.30/Kva	$ 1.30/Kva	"	$ 1.41	$ 1.45
Tariff L.C.P (Large Capacity Power)					
First 1,000 Kw Monthly Demand	$ 7.463	$ 6.673	$ 8.141	$ 7.261	$ 7.450
Next 3,000	$ 6.967	$ 6.177	$ 7.514	$ 6.722	$ 6.896
Over 4,000	$ 6.450	$ 5.660	$ 6.876	$ 6.159	$ 6.319
Energy in Excess of 315 Kwhrs Per Kw Demand	$ 0.01579	$ 0.01328	$ 0.0160426	$ 0.01461	$ 0.01506
Reactive Demand Charge	$ 0.25	$ 0.25	$ 0.32	$ .27	$ 0.28
Tariff I.R.P. (Interruptible Power)					
Demand Charge:					
Kw Demand	$ 0.676	$ 0.676	$ 0.841	$ 0.736	$ 0.755
Kvar Demand	$ 0.25	$ 0.25	$ 0.32	$ 0.27	$ 0.28
Energy Charge	$ 0.01499	$ 0.01248	$ 0.0149926	$ 0.01374	$ 0.01417

Notes:

* Not filed because of coincidental effectiveness of proposed No. 8182 rates.

** Filed rates adjusted for credit of .25074¢/KWH.

APPENDIX F—(Continued)

APPALACHIAN POWER COMPANY

Comparison of Rates

	I	II	III	IV	V
				Final Commission Approved Rates—Case No. 8182	
	Rates filed pursuant to order dated 8/9/76 in Case No. 7083. Reopened Effective 4/1/75-8/27/75	Lawful Base rates as of 8/27/75*	Net Rates filed in Case No. 8182**	Effective 8/28/75 through 4/30/76	Effective on and after 5/1/76
	¢/Kwh	¢/Kwh	¢/Kwh	¢/Kwh	¢/Kwh
Tariff H.L.P. (High Load Factor Power)					
For 34.5-69 KV Delivery Voltage					
First 67,000 KW Demand	$10.287	$ 8.783	$10.61456	$ 9.557	$ 9.805
Next 33,000 KW	$10.044	$ 8.540	$10.30656	$ 9.293	$ 9.534
Over 100,000 KW	$ 9.922	$ 8.418	$10.15856	$ 9.160	$ 9.397
For 138 KV Delivery Voltage					
First 67,000 KW Demand	$10.206	$ 8.701	$10.51156	$ 9.468	$ 9.714
Next 33,000 KW	$ 9.993	$ 8.488	$10.23856	$ 9.238	$ 9.477
Over 100,000 KW	$ 9.873	$ 8.368	$10.09056	$ 9.105	$ 9.341
Secondary—All Voltage					
Energy in Excess of 600 KWHrs per KW Demand	$ 0.01411	$ 0.01160	$ 0.0138720	$ 0.01279	$ 0.01318
Demand Charge	$ 0.25	$ 0.25	$ 0.32	$ 0.27	$ 0.28
Tariff O.L. (Outdoor Lighting)					
Each 7,000 Lumen Mercury	$ 4.22	$ 4.74	$ 5.92	$ 5.16	$ 5.29
Each 11,000 Lumen Mercury	$ 5.53	$ 6.25	$ 7.83	$ 6.80	$ 6.98
Each 20,000 Lumen Mercury	$ 6.59	$ 7.74	$ 9.81	$ 8.42	$ 8.64
Each 2,500 Lumen Incandescent	$ 3.16	$ 3.63	$ 4.58	$ 3.95	$ 4.05
Each 4,000 Lumen Incandescent	$ 3.69	$ 4.42	$ 5.65	$ 4.81	$ 4.93
Each 7,000 Lumen Mercury on 12′ Post	$ 5.00	$ 5.52	$ 6.87	$ 6.00	$ 6.16
Rider A (Credit Surcharge)					
Credit applied to RS, GS, CS, CP, CIP, PSO, EHG, TP, SS, LP, LCP, IRP & HLP for each Kwh used	$ .0000673	Not Applicable	Not Applicable	Not Applicable	Not Applicable

NOTE:

* Not filed because of coincidental effectiveness of proposed No. 8182 rates.

** Filed rates adjusted for credit of .25074¢/Kwh.

APPENDIX F—(Continued)

APPALACHIAN POWER COMPANY

Comparison of Rates

	I	II	III	IV	V
				Final Commission Approved Rates—Case No. 8182	
	Rates filed pursuant to order dated 8/9/76 in Case No. 7083. Reopened Effective 4/1/75-8/27/75	Lawful Base rates as of 8/27/75*	Net Rates filed in Case No. 8182**	Effective 8/28/75 through 4/30/76	Effective on and after 5/1/76
	¢/KWH	¢/KWH	¢/KWH	¢/KWH	¢/KWH
Tariff R.E. (Rural Line Extension)					
Tariffs Applied	Applicable Tariff	Applicable Tariff	Applicable Tariff	Applicable Tariff	
Minimums:					
Per Customer Per Month	$ 2.50	$ 2.50	$ 4.00	$ 4.00	$ 4.00
Per Mile Per Month	$ 10.00	$ 10.00	$ 18.50	$ 18.50	$ 18.50
Minimum Excluded if Gross Annual Revenue Per Mile Exceeds	$500.00	$500.00	$775.00	$775.00	$775.00
Tariff T.S. (Temporary Service)					
Tariffs Applied	Applicable Tariff	Applicable Tariff	Applicable Tariff	Applicable Tariff	
Special Terms	Available in Cases Where Provisions of Applicable Tariff Would Normally Preclude Service of a Temporary Nature.				

APPENDIX G

APPALACHIAN POWER COMPANY
(CASE NO. 8182)

Certain portions of the "Terms and Conditions of Service" in Appalachian's tariff filing designated W.Va. P.S.C. Tariff No. 3 in Original Sheet Nos. 3-1, 3-2, 3-3, 3-4 and 3-5 are to be modified as follows:

Original Sheet No. 3-1

"APPLICATION"—This paragraph shall be broadened to comply with Section 4.01 (2) and (3) of the "Rules and Regulations for the Government of Electric Utilities" (referred to hereinafter as the "Electric Rules") promulgated by the Commission as of March 1, 1977.

"DEPOSITS"—This paragraph shall be modified to conform with Section 4.02 of the Electric Rules of the Commission.

Original Sheet Nos. 3-1 and 3-2

"PAYMENTS"—This section shall be broadened to comply with Section 4.08 (1) (a) (4) of the Commissioner's Electric Rules requiring the utility to accept payment at the customer's premises in lieu of discontinuing service.

Original Sheet No. 3-2

"SERVICE CONNECTIONS"—This section shall be modified to exclude residential customers from the requirement that the customer's wiring shall be brought outside the building wall nearest the Company's service wires. Moreover, our ruling on this section, is subject to Order in pending Case No. 8455, involving the Company, which will be issued soon.

Original Sheet No. 3-3

"COMPANY'S LIABILITY"—This section is subject to our Order in pending Case No. 8455, which will be issued soon.

Original Sheet Nos. 3-3 and 3-4

"EXTENSION OF SERVICE"—This section shall be modified to contain the substance of Appalachian's tariff, Original Sheet Nos. 3-6 and 3-7 filed in Virginia as part of the Company's Va. S.C.C. Tariff No. 7, issued June 2, 1975.

Original Sheet No. 3-4

"USE OF ENERGY BY CUSTOMER"—This section shall be modified so as to (1) exclude residential customers from the requirement that customers shall not add to the equipment or load of the residence except by consent of the Company, (2) the Company shall be the "initial" judge, but *not* the "sole" judge as to the suitability of apparatus and appliances and (3) The Public Service Commission of West Virginia shall be the proper forum for any disputes under this section which cannot be satisfactorily settled between the Company and its customer.

Original Sheet No. 3-5

"POWER FACTOR OF LIGHTING EQUIPMENT"—This section shall be modified to comply with Section 5.07 of the Commission's Electric Rules.

"DOMESTIC SERVICE"—This section shall be modified to provide that larger motors may be served when in the Company's "initial", not "sole" judgment, the existing service facilities of the Company are adequate.

Original Sheet No. 3-5

"DENIAL OR DISCONTINUANCE OF SERVICE"—This section shall be modified (1) to excuse residential customers whose service is discontinued for reasons stated in the section from paying a minimum bill after such discontinuance, and (2) the section shall be modified to conform to Section 4.08 of the Commission's Electric Rules.

Sheet 2 of 2
(Appendix G)
[Continued]

"Reconnection Charge"—This section shall be amended to reduce the reconnection charge for residential and general service customers to $5.50 as was contained in the tariff provisions in effect prior to the Company's W. Va. P.S.C. Tariff No. 3, because of failure of proof.

"General"—This section shall be amended to refer to the Commission's Electric Rules, revised as of March 1, 1977, and to be effective May 16, 1977.

PUBLIC SERVICE COMMISSION OF WEST VIRGINIA

Charleston

At a session of the Public Service Commission of West Virginia, at the Capitol in the City of Charleston on the 9th day of May, 1977.

Case No. 8182

Appalachian Power Company, a corporation.

In the matter of increased rates and charges.

Corrective Order

Whereas, by order entered herein on May 6, 1977, certain typographical errors have been noted and should be corrected, as follows:

Page 3—Third line from bottom, change "makes" to "make";
Page 4—Tenth line from bottom, change "Column I" to "Column II";
Page 33—Last line, change "75.9%" to 75.5%" [sic];
Page 34—First line, change "12,340,468,000" to "12,240,468,000 [sic];
Second line, change "18.1%" to "or 10.9% of total growth";
Third line, change "26.7% [sic] to "or 13.6% of total growth";
Third line from bottom, change "interchang-" to "interchange-";
Page 42—Eighth line, change "above" to "below";
Appendix C—under part B — change "9.25%" to "9.35%";
Appendix D—Under "Recapitulation of Total Energy Sales", Percent Column, change "18.1%" to

"10.9%" for W. Va.; "26.7%" to "13.6%" for Virginia and "75.9%" to "75.5%" for FPC; and

Appendix E, Sheet 1 of 2—change percentage growth in 1974 residential sales "28.5%" to "56.9%".

and that in all other respects, the said order of May 6, 1977, shall remain in full force and effect.

A Copy.

Teste:

s/ S. Grover Smith, Jr.
S. Grover Smith, Jr.
Secretary

PUBLIC SERVICE COMMISSION OF WEST VIRGINIA

Charleston

At a session of the Public Service Commission of West Virginia, at the Capitol in the City of Charleston on the 29th day of July, 1977.

Case No. 8182

Appalachian Power Company, a corporation.
In the matter of increased rates and charges.

ORDER DENYING IN PART AND GRANTING IN PART PETITION FOR REHEARING, REOPENING OF THE RECORD, AND REARGUMENT AND CLARIFYING ORDER ISSUED MAY 6, 1977.

Post-Decisional Procedure

On May 6, 1977, this Commission issued its final order covering a multitude of subsidiary issues in ratemaking, which allowed some rate relief but not all of the rate relief requested and, among other things, ordered Appalachian Power Company to refund excess collections of revenues with interest thereon at the annual rate of 7¾%.

On May 16, 1977, Appalachian filed its Petition for Rehearing, Reopening of the Record, and Reargument, with affidavits of Gerald P. Maloney, Morris E. McCrary, Peter J. DeMaria and Michael Brown McNulty, officers or employees of Appalachian or its affiliates. On May 23, 1977, Appalachian filed supplementary affidavits of Gerald Blackmore and Morris E. McCrary.

Appalachian's Petition for Rehearing, etc., requested modification of the Commission's order of May 6, 1977, to the effect that

(1) the rates determined upon a 9.35% rate of return were too low;

(2) the Commission had erred in its disposition of subsidiary issues pertaining to (a) consolidated tax savings, (b) capacity equalization adjustment, (c) jurisdictional cost allocation;

(3) the Commission should permit Appalachian to have a Third-Tier Rate Level increase effective May 1, 1977, on the basis of (a) purported increases in its cost of coal, (b) purported wage increases which became effective April 1, 1977, and (c) its continuing investment in pollution control facilities after August 1975; and

(4) the Commission should modify ordering paragraphs 4 and 5 of its order, so as (a) to give Appalachian 15 days after final determination on the relief requested by its Petition for Rehearing, etc., and (b) to delay the completion of refunds to a date 60 days from the date revised tariff sheets are finally approved by the Commission.

In addition, representatives of Appalachian informally raised the question with the Staff of the Commission as to how incidental details of the filed tariff sheets, not commented upon specifically in the Commission order, should be treated when the utility files its tariff sheets in compliance with our order. These incidental matters will be taken up on our own motion as a clarification of our order issued May 6, 1977.

COMMENT

We turn now to a discussion of the issues raised.

Consolidated Tax Saving

Appalachian's contentions against the Commission's order on the issue of the proper adjustment to Federal income tax to reflect a test year sharing of tax savings from filing a consolidated tax return by its parent, American Electric Power, Inc., are based upon a misunderstanding or misrepresentation of our order.

Appalachian erroneously characterizes the staff method approved by our order,—that the "approach assumes that the Parent's tax loss and thus the savings enjoyed by Appalachian will increase in proportion to increases in Appalachian's taxable income". This is Appalachian's view, not that of the Commission and its staff.

The method approved by the Commission is to use the *actual tax savings* associated with filing consolidated income tax returns over a three-year period prior to the test period in order to calculate a reasonable allowance for consolidated tax savings in ratemaking. Because of the many variables involved and the difficulty in projecting actual income tax savings to be experienced in future tax periods, the Commission exercises its discretion and judgment to make a fair adjustment for this cost item.

The Commission did *not* use "$4,100,837 of consolidated tax savings which was determined by applying a percentage factor (23%) to Appalachian's pro forma taxable income to derive Appalachian's allocated portion of the tax loss generated by Appalachian's Parent". Contrary to Appalachian's erroneous statement, the Commission reflected a tax savings for Appalachian of $1,197,747 for the first-tier rates and $1,204,818 for the second-tier rates, *not* $4,100,837. The recital of "$4,100,837 tax savings allocated to West Virginia" on page 28 of our order issued May 6, 1977, refers to a dollar figure based on the higher rates the Company asked for, and *not* on the lower rates the Commission granted.

Appalachian's rejected approach baldly assumes a non-variable Parent tax loss, without any evidentiary support.

We reject Appalachian's contentions on this issue and rely on the principle that where a projection of future Federal income tax savings is not known and measurable, the averaging method of projecting a tax savings is a conservative and fair way of determining the same.

Capacity Equalization Adjustment

Appalachian contends against the Commission's adjustment to test year purchased power expense in crediting adjusted (higher) test year revenues due to a June 1975 rate increase under the "Capacity Equalization Agreement" regulated by the Federal Power Commission. Its argument is grounded on its belief that by becoming a net purchaser of AEP System power after the test year, it should not have its test year purchased power expenses decreased by adjusted revenues based on a known and measurable FPC rate increase in June 1975 in the AEP System's Capacity Equalization Agreement.

Adjustments to test year revenues and expenses in ratemaking are largely discretionary to the regulator. In order to avoid arbitrary decisions, regulators usually confine their adjustments to "known and measurable" changes in revenues and costs. We followed that principle in our treatment of this issue. Appalachian, on the other hand, wants us to refrain from exercising our discretion, because of post-test year changes in AEP System power supply and usage which are ephemeral, and, even if "known", are *not* "measurable" within the context of the test year used in this proceeding.

Appalachian erroneously argues that the Commission is bound by one method of cost apportionment; namely, the "non-jurisdictional revenues credit to cost of service" method. To the contrary, not only are there many valid methods of jurisdictional cost apportionment, but also Appalachian's argument violates the recent teachings of the Supreme Court of the United States, to the effect that while one regulatory jurisdiction may lack authority to fix rates in another jurisdiction, it may determine the costs and take into account the rates in the other jurisdiction, when it fixes the rates in its own jurisdiction. See *FPC vs Conway Corporation,* US , 96 S Ct 1999 (1976). Indeed, the

very purpose of jurisdictional cost apportionment, where there is multiple regulation of a company, is for each jurisdiction to determine for itself the *fair* burdens that the customers it protects shall bear. In exercising this responsibility each jurisdiction has a broad discretion to use or not to use any number of cost apportionment methods, and each is *not* necessarily bound by the methods used by other jurisdictions, either Federal or State. If the Public Service Commission of West Virginia is not free to accept or reject the "revenue credit" method of cost apportionment, it would have lost an important element of its rate regulatory powers by the *indirect* encroachment of another regulatory body, and this would be counter to the intent of the various statutes which separate Federal and State rate regulation responsibilities.

The essence of Appalachian's argument is that it insists that this Commission cannot make any adjustments to test year figures, unless it makes all of the adjustments which are favorable to Appalachian, even though the basis for the additional adjustments are not *measurable* within the context of the 1974 test year.

For example, Appalachian makes a loose statement in its Petition that

> "The fact that Appalachian became a *capacity* deficient company within the AEP Power Pool in 1975 is a known change which even without Modification No. 3 substantially *increased* the Company's production expense over the test year level."

To the contrary, our regulation of Appalachian in the concurrent Cabin Creek Plant Case No. 8961 informs us that Appalachian was not a *capacity* deficient company within the AEP Power Pool in 1975, but instead started to become a *net purchaser of kilowatt-hours of energy* from the AEP Pool.

Appalachian continues its slant by stating that

> "Because of the difficulty of quantifying all the associated changes for ratemaking purposes, Appalachian has never sought an adjustment for this known change for test year experience."

Thus, this admission contains the general truth that an adjustment of gross sales and gross purchase volumes of energy *for the future,* resulting in a shift for Appalachian to become a *net seller* rather than a *net purchaser* of system power, are not only unpredictable, but more important, would reflect a total change in Appalachian and in system power supply and usage and concomitant revenues and costs. The Commission made a reasonable adjustment based on a "known and measurable" change in the FPC rate contained in the Capacity Equalization Agreement. Although *future* allocations in ratemaking may increase production expenses by the "revenue credit" method, also in that *future* rate case Appalachian may have purchased more power under its Capacity Equalization Agreement which it would have resold to its customers at a profit.

We reject Appalachian's assertions on this issue and reconfirm our discretionary adjustment to the production cost component in our order of May 6, 1977.

Jurisdictional Cost Apportionment

Appalachian continues to object to a step in jurisdictional cost apportionment which assigns a small portion of its costs to its short-term, limited-term and unit-power sales which were served during the test year as part of the annual and peak requirements. Appalachian wants to credit the revenues from these FPC jurisdictional sales to its cost of service, in similar fashion as was done relative with net revenues from affiliates under the Capacity Equalization Agreement. We could have used this method but we exercised our discretion to use a cost apportionment

method based on *actual test year and peak hour usage* by the short-term, limited-term and unit-power customers.

We thoroughly discussed Appalachian's contentions on this issue in our order of May 6, 1977, except for Appalachian's new argument that

> ". . . on January 17, *1977*, the date of maximum demand on Appalachian's and AEP's systems this past winter, neither Appalachian nor American Electric Power made any short-term or limited-term sales."

Again, this is an indirect attempt by Appalachian to shift from a *1974* test year to one that would include January *1977*. In the context of a new rate case based on a new set of complicated circumstances, the method approved by the Commission would still be one of several valid methods of cost apportionment. In a test year, including a January 17, 1977 peak, under the method approved in this Case No. 8182, the short-term and limited-term customers would *not* be assigned a portion of Appalachian's *demand* costs if they took no power during the peak hour, but they would be the *commodity* costs on the basis of allocation factors determined from test year sales to them. However, in that next rate case we will look at *Appalachian's capacity* situation and if it has or soon anticipates increased capacity from its 1301 Project at New Haven, West Virginia, we may adopt a different method of cost apportionment, such as the Average and Excess Demand method which we ordered to be filed by ordering paragraph 7 of our order dated May 6, 1977.

We adhere to our findings and conclusions on this issue as set forth in our said final order.

Third-Tier Rates

Appalachian requests the Commission to establish higher *Third-Tier* rates to be effective on and after May 1, 1977. As a basis for this request it argues that its costs of (1)

coal, (2) labor, and (3) pollution control facilities are presently escalating over the cost increase adjustments we allowed in determining First-Tier rates for August 28, 1975, through April 30, 1976, and Second-Tier rates for May 1, 1976, through April 30, 1977.

Putting this request in perspective, we reiterate that the test year selected by the Company for Case No. 8182 was *1974*; unaudited *1975* data was received in evidence as an aid to assure ourselves of the reasonableness of our adjustments to 1974 test year data. The evidentiary hearings closed August 31, *1976*. We adopted the rare technique of establishing two sets of rates to be effective on and after two dates, because of the passage of time since the filed rates went into effect on August 28, 1975, and the date of our final order of May 6, 1977.

Appalachian now wants us to set higher rates in this Case No. 8182, for the period beginning May 1, 1977, on the basis of three cost component changes out of the multitude of revenue and cost changes that have occurred and are occurring as of July 1977.

We refuse to exercise our discretion to grant this request for many reasons, chief among which is that (1) the West Virginia customers of Appalachian deserve a modicum of rate stability, even if confined to the statutory lag period built in to our controlling statute, Code 24-2-4, and (2) the purported increased costs relied upon relate to the time periods too far beyond the end of the test period of 1974 to be the basis of a rate adjustment without entertaining a new test period study.

Appalachian recites increased fuel costs as a reason for higher Third-Tier rates. However, this ignores our caution at page 11 of our order issued May 6, 1977 that Appalachian "may be made to absorb any unreasonable differential between the price it pays for coal to its affiliated suppliers and to its non-affiliated coal producers". This is an issue

to be resolved in the future. Moreover, in monitoring monthly fuel costs of Appalachian's John Amos plant we have noted wide variations between the percentage ownership of the plant and the percentage of current monthly fuel purchases assigned to Appalachian. For example, for the fifteen-month period December 1976 through April 1977, the "swings" are as follows:

	Appalachian's Ownership Percentage	Appalachian's Fuel Cost Percentage	Differential
December 1976	69.735%	88.027%	18.292%
March 1977	65.550%	51.454%	(14.135%)

These circumstances raise substantial questions that are not susceptible to a *Third-Tier* rate solution in this Case No. 8182.

End Result

Even though our order issued May 6, 1977, balanced the various contentions according to sound regulatory principles and set Two-Tier rates on the basis of a 9.35% rate of return on rate base, Appalachian contends the rates set are too low.

Appalachian's argument rests on two misconceptions. First, it argues that its unaudited and unilateral view of its interest coverage as of March 31, 1977 is 1.99 times (199%) "eliminates Appalachian's legal ability to issue new mortgage bonds or debentures", because the issuance of such new debt requires at least 2.00 times (200%) interest coverage "for 12 consecutive months in the 15-month period immediately prior to the month in which the new debt securities are to be issued."

Second, Appalachian argues that a 9.35% *rate of return on rate base* "implies a return on common equity of but 12.8%", which, it contends, is too low on the evidence of *cost of capital on certain period-ended over-all capitalizations.*

These arguments are rejected as being based upon an unduly narrow view of the facts concerning interest coverage and a misconception of the relationship between the concept of *rate of return on rate base* in ratemaking and the concept of *cost of capital on capitalization* resulting from operations of a fiscal period.

The "interest coverage" test required to raise new debt funds from investors is *not* a test of "confiscation" in deciding whether rates are just and reasonable. The test is no more than a security device used to restrain a company from imprudent future debt financing. As the Commission said in *The Potomac Edison Company, Case No. 8280,* order issued April 25, 1977,

> "The Commission has not accepted and does not accept the proposition that the calculation of an interest coverage ratio and the resulting revenues requirement is a replacement for sound regulatory discretion. The revenue requirement to maintain any coverage ratio is greatly affected by changes in capital structure elemental components. The determination of what capital structure is appropriate for a utility has historically been left to management, and the Commission does not understand the Respondent as recommending otherwise. Therefore, we cannot accept the maintenance of a coverage ratio as a governing factor in ratemaking."

However, even if the "interest coverage" test was considered as an element in determining whether rates were or were not "just and reasonable", Appalachian's argument relying on *its* view of interest coverage on March 31, 1977, is not persuasive. Appalachian's earliest future debt financing would be late summer or early fall 1977. Any fifteen months period immediately prior to the month in which the new debt securities are to be issued, will include increased sales volumes, increased sales revenues due to growth and due to rate increases granted late in June 1977

by the FPC in its Docket No. ER77-325 and sought by Appalachian from the State Corporation Commission of Virginia through current hearings.

Moreover, Appalachian sought and secured approval for higher rates from this Commission on a 1974 test year having rate base costs and cost of service expenses relating to its Cabin Creek generating plant which is the subject of litigation before us and before the Federal courts. Whether or not this Commission prevails in its attempt to prevent Appalachian from prematurely discontinuing this plant from availability for service this coming winter or beyond, there appears to be no question that Appalachian will be able to reduce its costs associated with the Cabin Creek plant below the costs incurred during the test year 1974. To quantify this cost impact we will require Appalachian to provide this Commission with such data as an additional condition to our final order herein.

Finally, Appalachian's confusion in treating *cost of capital on end-of-period capitalization* as a strict determinant of *rate of return on rate base* in ratemaking has been thoroughly discussed at pages 22-25 of our final order herein. See also our discussion in *Hope Natural Gas Company, Case No. 8282,* order issued July 27, 1977, at pages 31-36.

We adhere to our belief that the "end result" of the rates we determined for Appalachian in our order issued May 6, 1977, are eminently just and reasonable.

Modification of Ordering Paragraphs 4 and 5

Appalachian requests that ordering paragraph of our order issued May 6, 1977, be modified to permit Appalachian to file revised tariff sheets 15 days "after final determination on the relief requested in this Petition", instead of 15 days from May 7, 1977. By filing its Petition for Rehearing, etc., seeking modification of ordering paragraph

4, Appalachian effectively tolled the running of the 15 days. We will modify our ordering paragraph 4, to require compliance on or before August 15, 1977.

Applicant requests that ordering paragraph 5 of our final order be modified to permit Appalachian to complete refunds within 60 days from the date such revised tariff sheets are finally approved. For similar reasons, we will modify our ordering paragraph 5 to require refunds to be complete within 60 days after our approval of the revised tariff sheets to be filed pursuant to this order and our order issued May 6, 1977. This means that if Appalachian files the revised tariff sheets on August 15, 1977, and we issue our order the same day approving same, that refunds will be required to be completed on or before October 14, 1977, unless our orders are stayed by a tribunal having jurisdiction so to do.

Clarifications

As additional guidance to incidental items not specifically mentioned in our order issued May 6, 1977, certain additional changes in the filed tariff sheets of W. Va. P.S.C. Tariff No. 3 are required as just and reasonable, consistent with our order, the record made and our recently effective "Rules and Regulations for the Government of Electric Utilities, 1977" as follows:

1. *Original Sheet No. 3-2*—Delete the last paragraph pertaining to a $2.00 or $10.50 service charge as not supported in the record by cost evidence, and see Electric Rule 5.06.

2. *Original Sheet No. 5-1, et al*—In the paragraph on "Equipment Supplied by Customer", change "$0.19" to "$0.17" per KW of monthly billing demand. Make the same adjustment in other schedules where applicable.

3. *Original Sheet No. 7-1, et al*—In the paragraph on "Equipment Supplied by Customer", change

"$0.32" to "$0.28" per KW of monthly billing demand. Make the same adjustment in other schedules where applicable.

4. *Original Sheet No. 10-1*—In the paragraph on "Adjustment of Demand Charge", modify "$0.00147" *to* "$0.00128 per KW of monthly billing demand [etc.]" for the period August 28, 1975, through April 30, 1976, and *to* "$0.00133 per KW of monthly billing demand, [etc.]" for the period May 1, 1976 forward.

5. *Original Sheet Nos. 5-1, 6-2, 7-2, 14 and 15*—Modify the "Payment" paragraph to change "fifteen (15)" to "twenty (20)" days and add a sentence "This delayed payment charge is not interest and is only to be collected once for each bill where appropriate."

6. *Original Sheet Nos. 8-2, 9-2, and 10-2*—Modify the "Payment" paragraph to change "fifteen (15)" to "twenty (20)" days, and change the last clause to read ". . . , customer shall pay Company a delayed payment charge on the total amount billed of 5% (but not less than $0.15). This delayed payment charge is not interest, and is only to be collected once for each bill when appropriate."

7. *Original Sheet Nos. 11-1, 16 and 17*—Modify the "Payment" paragraph to change "fifteen (15)" to "twenty (20)" days.

ORDER

A. The Commission denies Appalachian's request to reopen the evidentiary record, except that the Commission has fully considered the affidavits submitted by Appalachian with its Petition.

B. The Commission orders that paragraph 4 of its order issued May 6, 1977, be revised to extend the time to August 15, 1977, on or before which Appalachian shall file its revised tariff sheets in compliance with this order and our order issued May 6, 1977.

C. The Commission orders that paragraph 5 of its order issued May 6, 1977, be revised to extend the time for

Appalachian to complete its refunds within 60 days after the Commission's approval of the revised tariff sheets required to be filed by August 15, 1977.

D. The Commission hereby adds an ordering paragraph 8, to provide as follows:

8. Appalachian is hereby ordered to file on or before September 15, 1977, cost data for test year 1974 that would pertain both to rate base and over-all cost of service allocated to West Virginia which would be deducted if the Cabin Creek plant had not been in service during the test period 1974.

E. The Commission denies Appalachian's request to determine Third-Tier rates effective May 1, 1977, in this Case No. 8182, and

F. The Commission hereby affirms, as modified herein, its final order issued May 6, 1977.

s/ BROOKS E. SMITH
Chairman

PUBLIC SERVICE COMMISSION OF WEST VIRGINIA

CHARLESTON

At a session of the PUBLIC SERVICE COMMISION OF WEST VIRGINIA, at the Capitol in the City of Charleston on the 26th day of August, 1977.

CASE No. 8182

APPALACHIAN POWER COMPANY, a corporation.
In the matter of increased rates and charges.

WHEREAS, by order entered herein on July 29, 1977, the Commission denied in part and granted in part a petition filed May 16, 1977, for rehearing, reopening of the record, reargument, and clarification of its order issued May 6, 1977; and

WHEREAS, upon due consideration and goods [sic] reasons appearing therefor, the Commission is of opinion and finds that this case should be reopened, set for further evidentiary hearing, and reargument in order to enable the Commission to determine the reasonableness of a third tier rate level increase effective May 1, 1977, on the basis of respondent's purported increases in cost of coal.

IT IS, THEREFORE, ORDERED that this matter be, and it hereby is reopened for further evidentiary hearing for the reason and purpose as above stated, and it is hereby set for further hearing to be held in the Commission's Hearing Room at the Capitol in the City of Charleston on the 27th day of October, 1977, at 9:30 a.m., EDT, at which time and place the respondent shall appear and prosecute its interests herein, and anyone interested may appear and make such objections thereto as may be deemed proper.

IT IS FURTHER ORDERED that the Secretary of the Commission give notice of this proceeding to all parties of record by mailing to each of them a copy of this order by United States Certified Mail, return receipt requested.

Chairman McDonald, deeming himself disqualified, took no part in the consideration or decision of this matter.

A COPY.

TESTE:

s/ S. Grover Smith, Jr.
S. GROVER SMITH, JR.,
Secretary

PUBLIC SERVICE COMMISSION OF WEST VIRGINIA

CHARLESTON

At a session of the PUBLIC SERVICE COMMISSION OF WEST VIRGINIA at the Capitol in the City of Charleston on the 30th day of August, 1977.

CASE No. 8182

APPALACHIAN POWER COMPANY, a corporation.
In the matter of increased rates and charges.

By Commission order entered herein on July 29, 1977, Appalachian Power Company, a corporation, was ordered to file Revised Tariff Sheets by August 16, 1977 in compliance with our Order issued May 6, 1977 and our Order issued July 29, 1977. The Tariff Sheets to be effective August 28, 1975, through April 30, 1976, were to reflect rates and charges set forth in Appendix F of our Order of May 6, 1977, which rates and charges were sufficient to recover an additional $15,380,249 over the annual revenue level produced by rates which were in effect prior to August 28, 1975. The Tariff Schedules to be effective on and after May 1, 1976, were to reflect rates and charges specified in Appendix F of our Order of May 6, 1977, which rates and charges were sufficient to recover an additional $20,309,899 over the annual revenue level produced by rates which were in effect prior to August 28, 1975.

On August 15, 1977, Appalachian did submit to the Commission, Original Sheets of its P.S.C. W.Va. Tariff No. 3, cancelling its P.S.C. W.Va. Tariff No. 2, effective August 28, 1975 through April 30, 1976. Likewise, on August 15, 1977, Appalachian filed First Revisions of Original Sheets of its P.S.C. W.Va. Tariff No. 3, for service on and after May 1, 1976. The Tariffs were inspected by the Commission and were found to be generally in compliance with our

Orders of May 6, 1977 and July 29, 1977, except in the following instances:

(1) *Original Sheet No. 3-6 and First Revision of Original Sheet No. 3-6.*

Use of Energy by Customer

The paragraph beginning, "the customer shall install . . ." is not in compliance with the requirements of our Order dated May 6, 1977. This paragraph should be changed to read as follows:

> The customer shall install only motors, apparatus or appliances which are suitable for operation with the character of the service supplied by the Company, and which shall not be detrimental to same, and the electric power must not be used in such a manner as to cause unprovided for voltage fluctuation or disturbances in the Company's transmission or distribution system. While the Company may be the initial judge as to the suitability of apparatus or appliances, and also as to whether the operation of such apparatus or appliances is or will be, detrimental to its general service, the Public Service Commission of West Virginia shall be the proper forum for settling any disputes under this section which cannot be satisfactorily settled between the Company and its customer.

(2) *Original Sheet No. 3-6 and First Revision of Original Sheet No. 3-6.*

Domestic Service

The last sentence of the second paragraph should be changed to read as follows:

> Larger motors may be served when, in the Company's initial judgment, the existing service facilities of the Company are adequate; however, the Public Service Commission of West Virginia shall be the proper forum for settling any disputes under this section which cannot be satisfactorily settled between the Company and its customer.

(3) *Effective Dates*

The Tariff submitted by Appalachian for service on and after May 1, 1976, indicated that it was "Effective: October 1, 1977". The Commission finds this to be in error, and in view of our Order dated August 26, 1977 which reopens this case for limited purposes, such Tariff Schedules should be changed to read:

Effective: May 1, 1976 through April 30, 1977.

Except for the items pertaining to terms and conditions of service and effective dates of Tariffs, as hereinabove discussed, the Tariffs filed by Appalachian on August 15, 1977 are found to be in compliance with our Orders of May 6, 1977 and July 29, 1977.

IT IS THEREFORE, ORDERED that the rates and charges set forth in the Tariffs submitted by the respondent on August 15, 1977, shall be placed in effect on the dates specified in the aforementioned Commission Order of May 6, 1977.

IT IS FURTHER ORDERED, that Appalachian shall file Revised Schedules reflecting the terms and conditions of service and effective dates hereinabove prescribed within ten (10) days of the date of this Order.

IT IS FURTHER ORDERED, that the sixty (60) day maximum period allowed to the respondent, Appalachian Power Company to complete its refunds to its customers as set forth in paragraph five of the "ORDER" section of our order of May 6, 1977, and paragraph C of the "ORDER" section of our order of July 29, 1977, shall begin to run as of the date of this order.

Chairman McDonald, deeming himself disqualified, took no part in the consideration or decision of this matter.

A COPY.

TESTE:

s/ S. Grover Smith, Jr.
S. GROVER SMITH, JR.
Secretary

PUBLIC SERVICE COMMISSION
OF WEST VIRGINIA
CHARLESTON

At a session of the PUBLIC SERVICE COMMISSION OF WEST VIRGINIA at the Capitol in the City of Charleston on the 13th day of January, 1978.

CASE NO. 8182 (Reopened)

APPALACHIAN POWER COMPANY, a corporation.

In the matter of increased
rates and charges.

PROCEDURE

On March 31, 1975, APPALACHIAN POWER COMPANY, a corporation (hereinafter "APPALACHIAN"), filed its tariff designated P.S.C. W.Va. No. 3, cancelling P.S.C. W.Va. No. 2, stating increased rates and charges and certain modified rate designs for furnishing electric service in the entire territory served by it in the State of West Virginia, to become effective May 1, 1975. The filed tariff was suspended by order of the Commission and went into effect, subject to refund, on August 28, 1975. After hearings in July and August, 1975 and January, April, June, July and August, 1976, and after the filing of briefs in November, 1976, the Commission issued its decision in this case by order dated May 6, 1977.

On May 16, 1977, APPALACHIAN filed a petition for rehearing, reopening of the record, and reargument, along with affidavits of various officers and employees of APPALACHIAN and its affiliates. Only July 29, 1977, the Commission issued an order "denying in part and granting in part" APPALACHIAN'S petition, and on August 25, 1977, the Commission issued an additional order which reopened the record in Case No. 8182 for the purpose of taking further evidence in order to enable the Commission to determine the reasonableness of a "third-tier" rate level, effective May 1, 1977, on the basis of increased coal costs.

Proper notice was given and a hearing was held on October 27, 1977. At that hearing, APPALACHIAN was represented by Samuel M. Sugden and David M. Flannery, Attorneys at Law. The Staff was represented by Clement R. Bassett and George Zivkovich, Attorneys at Law, Legal Division; David J. Ellis, Robert C. Stier and Herlman Gibson, Division of Accounts, Finance and Rates; and C. William Wensyel, Division of Engineering. Attorneys for various intervenors were: T. D. Kauffelt, representing FMC Corporation; Michael T. Chaney, representing the City of Charleston and the City of South Charleston; John C. Lobert, representing ACF Industries, Inc., American National Rubber Company, Houdaille Industries, Inc., Huntington Alloys, Inc., Chemtron Corporation and Owens-Illinois, Inc.,; Robert Carr, representing the City of Princeton and Robert R. Rodecker, representing Appalachian Research and Defense Fund, Inc., Mercer County Economic Opportunity Corporation and McDowell County Consumer Action Council, Inc.

Company testimony was adduced from four witnesses and staff testimony from two witnesses.

Certain data requests made during the hearing, designated Respondent's Exhibits 1-B, 1-C, 1-D, and 1-E were received on November 7, 1977. APPALACHIAN'S brief was filed on November 28, 1977.

ISSUES

This proceeding is limited to the question of the propriety of the Commission's establishment of a "third-tier" rate level, effective May 1, 1977, in recognition of APPALACHIAN'S increased coal costs over those cost levels reflected in the Commission's Order of May 6, 1977. In that Order the Commission established two rate levels, based on two separate costs of service. The "first-tier,"

effective August 28, 1975 through April 30, 1976 provided for a revenue increase of $15,380,249 over rate levels effective prior to August 28, 1975 and included coal expense of $1.00 per Mbtu. The "second-tier," effective on and after May 1, 1976, provided for a revenue increase of $20,309,899, and included an allowance for coal expense at $1.04 per Mbtu.

APPALACHIAN presented evidence that "per books" coal costs were as follows:

	COST PER MBTU $
May, 1977	1.14
June, 1977	1.15
July, 1977	1.19
August, 1977	1.22
September, 1977	1.28

APPALACHIAN'S witness further estimated coal costs for October, 1977 at $1.33, a level which was projected to remain constant through the end of 1977. APPALACHAIN'S Exhibit 1-B, filed November 7, 1977, reflected actual October, 1977 coal costs as $1.32 per Mbtu.

APPALACHIAN did not specifically offer testimony as to the level of coal expense that should be reflected in a "third-tier" cost of service; but rather, presented testimony that an additional allowance for coal costs of $19,517,000 would be required for the period May, 1977 through February, 1978. The calculation of this number was based on a comparison of actual May through September, 1977 coal costs and projected October, 1977 through February, 1978 costs for the $1.04 per Mbtu reflected in Commission approved "second-tier" rate levels. APPALACHIAN used a heat rate of 9,500 Btu per

Kwh, a 7½% line-loss factor and a 3% hydrogeneration factor to convert its coal costs per Mbtu to a rate requirement per Kwh sold. Since the company filed rates in Case No. 8182 would produce approximately $17,000,000 over and above Commission approved "second-tier" rate levels during the same period, it is the company's position that the Commission should approve its originally filed rate levels, effective May 1, 1977.

Staff Exhibits were generally in agreement with the company's Exhibits with regard to the "per books" cost of coal in the months of May, June, July and August, 1977. Staff, however, took the position that APPALACHIAN'S book costs included coal purchased from affiliates at cost levels which were too far above nonaffiliated costs to be dismissed by the Commission in this proceeding. Staff Exhibits show that from May, 1976 through April, 1977, the differential between total book costs and coal costs at levels of purchases from nonaffiliates, ranged from 1.3¢ per Mbtu to 8.9¢ per Mbtu, with the average differential being 4.7¢ per Mbtu. Staff Exhibits further show that from May through August, 1977, the excess of booked coal costs including higher priced affiliated coal over cost levels of coal purchased from nonaffiliates continued to widen to a level of approximately 12¢ per Mbtu. In August, 1977 the weighted average cost of coal per books was $1.23 per Mbtu, whereas coal purchased from companies not affiliated with APPALACHIAN POWER COMPANY cost an average of $1.11 per Mbtu.

A review of the montly coal purchase summaries, which were set up by this Commission as a result of legislative requirements, clearly shows the growing disparity between APPALACHIAN'S purchases from affiliates and nonaffiliates during the last half of 1976 and the first half of 1977.

The question of the cost level of APPALACHIAN'S purchases from its affiliates, and the extent to which excess affiliated costs over non-affiliated should be reflected in rates, was not first raised in this proceeding. For many years prior to this Commission's dissallowance of automatic fuel adjustment clauses, APPALACHIAN was required to reflect coal costs based on nonaffiliated prices only in calculating its fuel cost adjustment in West Virginia. The record in this case is clear that APPALACHIAN was not allowed to recover all of this affiliated coal costs in the State of West Virginia in 1977 because of the excess of affiliated cost over nonaffiliated cost. For many years, the Commission has been told by APPALACHIAN that coal produced by its affiliates should be available to APPALACHIAN at prices that are the same or lower than coal purchased from nonaffiliates. In our Order in Case Nos. 7930, 8354, 8358, and 8359, the Commission discussed at length the disparity between purchases from affiliates and nonaffiliates. In our Order in Case No. 8182, we expressed our concern that representations of "same or lower priced" coal from affiliates were not being actually experienced by APPALACHIAN POWER COMPANY. While we agree, as pointed out by APPALACHIAN in its brief, that we have in the past acted favorably with regard to APPALACHIAN'S expansion of its coal mining affiliates, it has always been after consideration of the company's repeated assurances of its ability to purchase its affiliate's coal output at costs which compare favorably to costs available from nonaffiliated suppliers.

In contrast to "per books" costs as previously outlined, the Staff presented evidence which showed that APPALACHIAN'S average cost of coal purchased from nonaffiliates was as follows:

	COST PER MBTU $
May, 1977	1.05
June, 1977	1.05
July, 1977	1.09
August, 1977	1.11

Based on this data, the Staff recommended that the Commission provide a third-tier of rates effective May 1, 1977 which departed from the previously approved "second-tier" rate level only to the extent of raising the coal expense included in the cost of service from $1.04 per Mbtu, to $1.08 per Mbtu.

The Commission agrees with the Staff position that the Company must be held accountable for higher costs of affiliated coal; and that requiring West Virginia ratepayers to reimburse APPALACHIAN for its purchases from affiliates, regardless of their cost level, would be a disincentive to prudent and efficient operation of the coal mining affiliates. On the other hand, we must recognize that the rates established herein are for the "locked-in" period from May 1, 1977, until the rates go under bond in Case No. 9091, and should be sufficient to allow APPALACHIAN POWER COMPANY to recover reasonable costs incurred under the regulation of a competitive market place. We will therefore approve a "third-tier" rate level, effective May 1, 1977 which includes an allowance for coal expense at a level of $1.16 per Mbtu. (See Appendix A).

Cost of service components and revenue deficiency are set forth in Appendix A. Staff has prepared rate schedules in Appendix B in conformity with the findings and conclusions set forth in this decision.

FINDINGS

1. Respondent's rates and charges last approved by this Commission are unjust and unreasonable in that they will not produce sufficient revenues to enable the Respondent to pay its reasonable and necessary operating expenses and taxes, provide for depreciation, and earn a fair return on its property used and useful in its public service business for the period beginning on and after May 1, 1977 and until the rates go into effect in Case No. 9091.

2. Respondent's rates and charges, now in effect under bond, are likewise unjust and unreasonable in that they would produce more revenues than are needed for the aforesaid purposes and period.

3. The rates and charges hereinafter approved are just and reasonable in that they should produce revenues sufficient, but not more than sufficient, for the aforesaid purposes and period. (Appendix B).

ORDER

1. The rates and charges that Respondent now has in effect under bond for the above said period are hereby cancelled and stricken from the tariff files of the Commission.

2. The rates set out in Appendix B that is hereto attached, be approved, to become effective May 1, 1977.

3. The Respondent shall refund to the person or parties entitled thereto, within sixty days (60) days of the date of this order, the amount of excess collected under the rates placed into effect under bond, and the amount which would have been collected under the rates that are herein approved, with interest at the rate of seven and three-

quarters per cent (7¾%) per annum, until paid; that refunds of Five Dollars ($5.00) or less may be made by crediting the amount to the subscriber's account, and that as to amounts in excess of Five Dollars ($5.00), the refund shall be made by check.

The Respondent shall report to the Commission the amount refunded, including the interest, the manner of refunding, and the amount if any, which it has been unable to refund.

4. Respondent shall file with the Commission, within fifteen (15) days from the date of this order, tariff sheets stating its rates and charges as specified herein.

5. Chairman McDonald, deeming himself disqualified, took no part in the consideration or decisions of this Case.

A COPY

TESTE:
Freeda P. Jones
Acting Secretary

APPENDIX A

APPALACHIAN POWER COMPANY

CASE NO. 8182 (REOPENED)
COST OF SERVICE COMPONENTS AND REVENUE DEFICIENCY PER COMMISSION ORDER
TEST YEAR 1974
WEST VIRGINIA OPERATIONS
THIRD TIER

A. Cost of Service Components

	Operating Revenues	Operating Expenses	Depreciation And Amortization	Taxes Other Than Federal Income Tax	Average Rate Base
	$	$	$	$	$
As Adjusted for Period From April 30, 1976 thru April 30, 1977 ..	176,075,074	111,317,884	17,334,859	16,216,009	488,976,907
Adjustments:					
Coal Expense 1.16¢ per MBTU ...		9,127,299			
As Adjusted	176,075,074	120,445,183	17,334,859	16,216,009	488,976,907

B. Cost of Service and Revenue Deficiency

Allowance for Return 9.35%	$ 45,719,341
Operation and Maintenance Expense	120,445,183
Depreciation and Amortization	17,334,859
Federal Income Tax.	4,596,410 *
Other Taxes — Before Additional Business & Occupation Tax	16,216,009
Additional Business & Occupation Tax	1,654,969 *
TOTAL COST OF SERVICE	$205,966,771
REVENUE DEFICIENCY	$ 29,891,697

* Calculated after other adjustments.

APPENDIX B

APPALACHIAN POWER COMPANY

CASE NO. 8182 (REOPENED)

	Approved Rates Effective May 1, 1977 ¢/Kwh
Tariff C.L.P. (Combined Light & Power)	
Primary (50 x Capacity)	
Secondary (Excess over Primary)	
First 5,000 Kwhrs	
Next 5,000 Kwhrs	Discontinued
Over 10,000 Kwhrs	
Minimum Charge	
Tariff R.S. (Residential Service)	
First 30 Kwhrs per month	6.025
Next 40	5.583
Next 130	3.773
Next 300	2.755
Next 1,000	2.416
Over 1,500	2.189
Minimum	$ 2.50
Water Heater Service	
Last 400 Kwhrs per month	2.189
Tariff G.S. (General Service)	
50 x Monthly Demand	
First 30 Kwhrs	6.737
Over 30	5.324
Next 150 x Monthly Demand	
First 3,000 Kwhrs	3.796
Over 3,000	2.778
Over 200 x Monthly Demand	2.212
Minimum Charge	$ 2.50

	Approved Rates Effective May 1, 1977 ¢/Kwh
Tariff C.I.P. (Commercial-Industrial) formerly C.P.O. (Capacity Power-Optional)	
First 30 x Monthly Demand	6.064
Next 170 x Monthly Demand:	
First 3,000 Kwhrs	3.496
Next 3,000	3.271
Next 4,000	3.044
Next 10,000	2.818
Next 80,000	2.592
Over 100,000	2.365
Next 160 x Monthly Demand	1.924
Over 360 x Monthly Demand	1.698
Minimum Charge	$ 2.00/Kva
Tariff P.S.O. (Public School-Optional)	
All Energy	3.910
Minimum Charge	$ 2.50
Tariff E.H.G. (Electric Heating General)	
First 200 Kwhrs	4.475
Next 6,800	2.778
Over 7,000	2.439
Each KW Demand in Excess of 30	$ 1.42
Minimum Charge	$ 8.74
Tariff S.S. (School Service)	
First 500 Kwhrs per Classroom	3.910
Balance	1.873
Minimum Charge	$ 2.50
Tariff C.S. (Church Service)	
First 40 Kwhrs per month	6.737
Next 85	5.606
Next 375	4.136
Next 500	3.118
Over 1,000	2.778
Minimum Charge	$ 2.50

	Approved Rates Effective May 1, 1977 ¢/Kwh
Tariff C.P. (Capapcity Power — Wholesale)	
100 x Contract Capacity:	
100 x First 50 Kva	4.640
100 x Next 50 Kva	4.186
100 x Next 50 Kva	3.055
100 x Next 150 Kva	2.830
100 x Over 300 Kva	2.603
Excess of 100 x Capacity:	
First 50,000 Kwhrs	2.592
Next 50,000	2.478
Next 200,000	2.365
Over 300,000	2.310
Minimum Charge	$26.80
Tariff T.P. (Transmission Power)	
For 34.5-69 KV Delivery Voltage	
First 25,000 KVA Demand	$ 6.250
Over 25,000 KVA Demand	$ 5.978
For 138 KV Delivery Voltage	
First 25,000 KVA Demand	$ 6.092
Over 25,000 KVA Demand	$ 5.922
Secondary — All Voltage	
Energy in Excess of 300 Kwhrs per KVA Demand	$ 0.01467
Tariff L.P. (Large Power)	
First 30 x Monthly Demand	6.061
Next 170 x Monthly Demand:	
First 3,000 Kwhrs	3.493
Next 3,000	3.268
Next 4,000	3.041
Next 10,000	2.814
Next 80,000	2.589
Over 100,000	2.362
Next 160 x Monthly Demand	1.921
Over 360 x Monthly Demand	1.695
Minimum Charge	$ 1.45

	Approved Rates Effective May 1, 1977 ¢/Kwh
Tariff L.C.P. (Large Capacity Power)	
First 1,000 KW Monthly Demand	$ 7.773
Next 3,000	$ 7.219
Over 4,000	$ 6.642
Energy in Excess of 315 Kwhrs Per KW Demand	$ 0.01613
Reactive Demand Charge	$ 0.28
Tariff I.R.P. (Interruptible Power)	
Demand Charge:	
KW Demand	$ 0.755
KVAR Demand	$ 0.28
Energy Charge	$ 0.1524
Tariff H.L.P. (High Load Factor Power)	
For 34.5-69 KV Delivery Voltage	
First 67,000 KW Demand	$10.420
Next 33,000 KW	$10.149
Over 100,000 KW	10.012
For 138 KV Delivery Voltage	
First 67,000 KW Demand	$10.329
Next 33,000	10.091
Over 100,000	9.956
Secondary — All Voltage	
Energy in Excess of 600 Kwhrs per KW Demand	$ 0.01425
Demand Charge	0.28
Tariff O.L. (Outdoor Lighting)	
Each 7,000 Lumen Mercury	$ 5.37
Each 11,000 Lumen Mercury	6.99
Each 20,000 Lumen Mercury	8.76
Each 2,500 Lumen Incandescent	4.06
Each 4,000 Lumen Incandescent	4.94
Each 7,000 Lumen Mercury on 12' Post	6.17

	Approved Rates Effective May 1, 1977 ¢/Kwh
Rider A (Credit Surcharge) Credit applied to RS, GS, CS, CP, CIP, EHG, TP, SS, LP, LCP, IRP & HLP for each Kwh used	
Tariff R.E. (Rural Line Extension)	
Tariffs Applied	Applicable Tariff
Minimums:	
Per Customer Per Month	$ 4.00
Per Mile Per Month	18.50
Minimum Excluded if Gross Annual Revenue Per Mile Exceeds	$775.00
Tariff T.S. (Temporary Service)	
Tariffs Applied	Applicable Tariff
Special Terms	Available

Supreme Court, U. S.
FILED
FEB 15 1978
DAK, JR., CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-979

APPALACHIAN POWER COMPANY,
Appellant,

v.

THE PUBLIC SERVICE COMMISSION OF WEST VIRGINIA,
Appellee.

ON APPEAL FROM THE SUPREME COURT OF APPEALS
OF THE STATE OF WEST VIRGINIA

BRIEF OPPOSING MOTION TO DISMISS OR AFFIRM

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February 15, 1978

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ON APPEAL FROM THE SUPREME COURT OF APPEALS OF THE STATE OF WEST VIRGINIA

BRIEF OPPOSING MOTION TO DISMISS OR AFFIRM

Appalachian Power Company ("Appalachian" or "the Company") hereby opposes the Motion to Dismiss or Affirm ("Motion") filed by the West Virginia Public Service Commission ("the Commission") in response to Appalachian's Jurisdictional Statement.

The Motion never once addresses the central issue—the end result of the Commission's rate orders is to leave Appalachian in a position where it is unable to raise the money necessary for the proper discharge of its public duties. It cannot even legally issue additional long-term debt or preferred stock and, since common stock is the most expensive type of capital, Appalachian obviously cannot meet its capital needs from this source.

INTRODUCTION

It is important to emphasize at the outset that there appears to be agreement between the parties on the essential facts. The Commission does not dispute Appalachian's requirement to spend more than $1 billion during the next three years in order to provide safe and reliable electric service to more than 678,000 customers in West Virginia and Virginia. Nor does the Commission dispute the fact that the end result of its decision is that Appalachian is precluded from legally issuing additional long-term debt securities or preferred stock, the types of capital least expensive to the ratepayers, to finance this $1 billion construction program. Also, in its Motion the Commission explicitly agrees with the Company's evaluation of its credit standing—the lowest of any major electric utility in the United States. The dispute between the Company and the Commission centers on the significance of these facts in evaluating the rate orders of the Commission in this proceeding under the standard of constitutional reasonableness articulated by this Court over more than 50 years.

Notwithstanding the many diversionary ploys contained in the Commission's voluminous Motion, this Court is not being asked to sift through a complicated factual situation to review findings of fact made by an administrative agency. The essence of this appeal is that the Commission failed to apply the proper constitutional standard; in misinterpreting or ignoring decisions of this Court in *Bluefield Water Works & Improvement Company* v. *Public Service Commission of West Virginia,* 262 U.S. 679 (1923) (*"Bluefield"*), and *Federal Power Commission* v. *Hope Natural Gas Company,* 320 U.S. 591 (1944) (*"Hope"*), the Commission violated Appalachian's constitutional right to rates which are adequate to permit the Company to attract the capital necessary to provide safe and reliable public utility service.

There are at least two substantial federal questions presented in this appeal. First, the Commission's decision effectively repudiates the capital attraction standard established in *Bluefield* and *Hope,* a result which, if applied in other regulatory jurisdictions, would have disastrous consequences for investor-owned public utilities and ultimately could bring about their extinction. Second, if allowed to stand, the Commission's decision will have an immediate detrimental burden on interstate commerce, affecting directly the reliable supply of electricity to the citizens of West Virginia, Virginia and Tennessee, and indirectly electric service to a large segment of the population in numerous other states.

In its attempt to defend its decisions in this case, the Commission has presented many justifications not considered in its orders below, many of which involve erroneous or misleading statements, or proffered "facts" for which there is no record support. For example, in its Motion the Commission suggests that the Company is excessively leveraged (pp. 25-26); that the Company's problems are the result of poor or imprudent management (p. 30); that the Company chose to increase debt at a time when interest rates are highest (p. 30); that the Company inflated its depreciation expense (p. 37); that the Company could increase earnings for coverage purposes by utilizing a consolidated income statement (p. 37); that the Company's method of financing its construction may not be the most efficient (p. 44); and that the Company should sell portions of its affiliated coal properties in order to raise needed capital (p. 45). All of these arguments have two common defects—they are raised for the first time and they are wrong. The Court should not be misled by the Commission's *post hoc* rationalizations for its actions. As this Court noted in *Securities and Exchange Commission* v. *Chenery Corporation,* 332 U.S. 194 at 196 (1947):

> [A] reviewing court, in dealing with a determination or judgment which an administrative agency alone is authorized to make, must judge the propriety of such action solely by the grounds invoked by the agency. If those grounds are inadequate or improper, the court is powerless to affirm the administrative action by substituting what it considers to be a more adequate or proper basis.

The importance of these substantial federal questions to the citizens of Virginia is eloquently emphasized in the Brief of the Commonwealth of Virginia as Amicus Curiae ("Virginia Brief") in requesting this Court to assume jurisdiction and grant the appeal in this case. The actions of the West Virginia Commission have so eroded the private rights of Appalachian as to pose a real and immediate danger to the public rights of hundreds of thousands of citizens of the Commonwealth of Virginia. As such, this proceeding has assumed the substance if not the form of a controversy between states whose importance ". . . transcends the immediate financial integrity and credit standing of Appalachian."[1]

I

THE COMMISSION FAILED TO APPLY THE CONSTITUTIONAL STANDARDS ENUNCIATED IN *BLUEFIELD* AND *HOPE*.

While never disagreeing that the end result of its orders is to eliminate Appalachian's ability to issue additional senior securities, the Commission at several points argues that the minimum constitutional requirements of public utility rates are effectively below minimum legal coverage requirements and thus coverage requirements are not embraced by the Fifth and Fourteenth Amendments to the

1 Virginia Brief, p. 3.

Constitution;[2] that Appalachian's coverage problems are a result of the Company's capital structure and not the Commission's rate decision;[3] and, repeatedly, that the allowance of a 9.35% rate of return, designed to produce an overall return of $46 million annually, amounts to an irrefutable determination of the constitutionality of the Commission's decision.[4] The common thread of all of these arguments is that Appalachian's ability to attract or even legally issue additional senior capital is irrelevant to the determination of a fair and reasonable rate of return. None of these propositions is well-founded.

Contrary to numerous statements contained in the Commission's Motion, the Company does not contend that 2.0 times interest coverage or any particular coverage level is a constitutional requirement. Rather, the gravamen of Appalachian's argument is that bond indenture and preferred stock coverage levels *do* represent an objective, easily calculable and absolutely minimum measure of the Company's ability to attract the additional capital needed to fund its construction program, and in that sense represent an essential element in the capital attraction standard of constitutional reasonableness set forth in the *Bluefield* and *Hope* decisions.

The necessity of meeting certain minimum coverage requirements prior to issuing additional senior securities is for Appalachian a matter of law pursuant to regulations of the Securities and Exchange Commission under Sections 6 and 7 of the Public Utility Holding Company Act of 1935 ("Holding Company Act") and also is a matter of private contract between the Company and the holders of more than $800 million of its outstanding debt securities. The minimum debt coverage requirement of course is not the

2 Motion, pp. 8, 11, 19.

3 *Id.*, pp. 22-32, 35-38.

4 *Id.*, pp. 9, 10, 18, 31.

2.0 times annual interest charges so frequently referred to in the Commission's Motion, because the interest which must be covered twice over is the sum of the outstanding interest *plus* the interest on the new debt to be issued.[5] The requirement of private contract law is similar to that of the vast majority of indentures of investor-owned electric utilities in the United States; the requirement of the Securities and Exchange Commission applies uniformly to all companies in public utility holding company systems registered under the Holding Company Act.

The Commission's argument that coverage is not relevant to the constitutionality of public utility rates would, if accepted by this Court, effectively reverse more than 50 years of precedent including *Bluefield* and *Hope*. Those cases and numerous others unequivocally establish that the ability to attract capital is a requirement which must be satisfied if public utility rates are to pass constitutional muster. If "ability to attract capital" has any vitality, it necessarily must embrace meeting the minimum legal criteria to issue long-term debt and preferred stock, the two least expensive types of permanent capital.

The conglomeration of peripheral arguments presented by the Commission in its Motion makes no attempt to meet the essential capital attraction issue. For example, the Commission's suggestion that a 9.35% overall rate of return calculated to produce $46 million of "net operating profits" *a priori* makes its decision constitutional, fails to consider other equally vital aspects of the ratemaking calculus and ignores the end result test established in *Hope*. A rate of return by itself is a meaningless number.[6] In

5 Obviously a bare minimum indenture coverage of 2.0 times annual interest requirements or a slim additional margin is not an appropriate level of coverage and will not maintain the financial integrity of the Company. It is only a requirement below which *no* additional long-term debt may be issued.

6 The comparison to rate of return allowed in Virginia is equally meaningless.

order for any rate of return to assume significance in the light of the utility's earnings it must be measured against the utility's investment (rate base) after giving full consideration to all operation and maintenance expense, depreciation, and taxes. A utility's ability to attract capital can be deprived just as easily by measuring a seemingly fair rate of return against a rate base which is far less than the utility's current investment, or by understating expense below that actually incurred, or by imputing revenues at higher than actual levels, or by establishing an improper class of non-jurisdictional customers, or by making the rates so established effective two or three years after the year in which the investment is measured. The interaction of the various elements of the rate-making process has worked in this case to deprive Appalachian of even approaching the earnings levels suggested by the Commission. While the Commission at numerous instances insists that its decision provides $46 million of West Virginia jurisdictional "net operating profits", the fact—of which the Commission is well aware—is that Appalachian's *total-company* net earnings for common in 1977 were less than $40 million, a return on equity of less than 8%.

Clearly within any individual part of the total ratemaking calculus a regulatory agency has broad discretionary authority. However, when the sum of its actions — the end result — fails to result in rates sufficient to permit the utility to attract any additional long-term debt capital or preferred stock capital, the Commission has overstepped its otherwise broad discretionary authority and transgressed into the area of unconstitutional confiscation of property.

There can be no better test of the end result than minimum legal coverage tests. Those tests are objective arithmetical exercises, calculated from actual per-books results and cost of securities to be issued, and require no judgment or expertise.

II

THE COMMISSION'S *POST HOC* RATIONALIZATIONS ABOUT COVERAGE ARE MISLEADING AND INACCURATE, AND SHOULD BE REJECTED BY THIS COURT.

At numerous points throughout its Motion, the Commission introduces extraneous and erroneous examples of coverage calculations not included in the evidentiary record or the Commission's decisions. Without ever denying the fact that the end result of its orders is to eliminate Appalachian's legal ability to issue additional senior capital, the Commission attempts to show that this end result is the product of the Company's and not the Commission's action, and that rate regulation which would afford Appalachian the legal ability to issue additional senior capital would result in excessive returns on common equity. These examples are misleading and obviously intended deliberately to confuse the clear-cut issues which are presented in this appeal.

The Commission's Motion continuously confuses operating income before taxes, operating income after taxes, coverages on the two different bases, and net earnings for common after interest expense and preferred dividends. For example, the Commission ignores the fact that the legal coverage test which Appalachian must meet is based on net earnings before interest and *income taxes*. Thus the final column at page 33 of the Motion grossly overstates the net earnings for stockholders which would, of course, be on an after-tax basis. Similarly, the entire textual example at page 34 of the Motion makes no provision for the income taxes associated with $56 million of net earnings available for common equity and accordingly completely misstates the coverage result. Moreover, even if the example had correctly reflected the appropriate allowance for income

taxes, the suggestion that the Company's annual interest expense would double without any corresponding change in the level of equity investment is so simplistic and naive as to make the example meaningless.

The Commission suggests[7] that coverage could be improved by reducing depreciation expense or taxes (other than income taxes) without indicating a means or rationale for understanding the former or evading the latter and, indeed, the Commission challenged the levels of neither item on the record in this case.

The Commission repeatedly argues that the Company is highly debt leveraged, and thus management has created its own coverage problems which should not be resolved by Commission action. The Commission's arguments must be rejected. The percentage of debt subject to the Company's debenture coverage test is presently lsss than 54% of Appalachian's total capitalization, a level comparable to the electric utility industry average debt ratio. The Commission's misleading statement that Appalachian's debt ratio is 61%[8] ignores the fact that the Company's debt (reflected in the 61%) includes more than $100 million of capitalized instalment purchase contracts associated with tax-exempt revenue bond pollution control financings (approximately 7% of the capital structure) which is not treated as long-term debt for coverage purposes. Similarly, the Commission states that "Appalachian's senior capital as a percentage of total capital has ranged from 67.51% to 70.23%,"[9] implying erroneously that this is significantly related to the Company's interest coverage calculations. Table 3 at page 27 of the Motion indicates that the Commission has included capitalized installment purchase contracts, short-term debt and preferred stock in the "senior

7 Motion, p. 23.

8 *Id.*, p. 36.

9 *Id.*, p. 26.

capital" calculation, none of which affects the coverage test for issuing new long-term debt. Indeed, Table 3 illustrates that the Company's common equity ratio has increased, albeit modestly, over the five-year period. Thus, when the Commission states that "Appalachian has obviously chosen to increase debt at a time when interest rates are highest,"[10] Table 3 confirms that the Commission is misrepresenting the facts to this Court. There has not been an increased use of long-term debt, but simply a continued *pro rata* division among the various sources of capital of the total financing requirements needed to cover the costs of new capital expenditures and, actually, a *reduction* in the percentage of total capital represented by long-term debt subject to the interest coverage test. Presumably, the Commission would have the Company alter its capital structure by issuing additional common equity to finance its construction program. The Commission is oblivious to the fact that a company which cannot even legally attract less costly debt or preferred equity is simply unable to attract common equity in the substantial amounts required.

At numerous points the Commission attempts to disclaim any regulatory authority over Appalachian's capital structure, simply because it lacks statutory authority to approve the Company's security offerings. Such disclaimers should be given no weight by this Court. The Commission in recent rate proceedings has had ample opportunity to seek to modify the Company's capital structure by imputing a different capital structure for ratemaking purposes.[11] Instead, the Commission has accepted for ratemaking pur-

10 *Id.*, p. 30.

11 In numerous instances where regulatory commissions have believed that a utility's equity capitalization was too high, the commission has reduced the ratio for ratemaking purposes. See *In the Matter of Communications Satellite Corporation*, 56 F.C.C.2d 1101, 1157-1158 (1976); *Re New England Teleph. & Teleg. Co.*, 13 P.U.R. 4th 65, 68-69 (Me. P.U.C. 1976).

poses the Company's actual capitalization and saved its arguments about leverage for judicial appeals. Appalachian's capital structure is within the capital structure standards approved by the Securities and Exchange Commission under the Holding Company Act and each issuance of Appalachian's long-term debt and preferred or common stock is authorized by the Securities and Exchange Commission after public notice. Thus, in light of the Company's actual capital structure, the Commission's "reasonable modification"[12] is absurd. The Company's actual debt ratio subject to the coverage test was already below 54% at the end of 1977, and, after reflecting the total impact of all of the Commission's actions in the instant case, Appalachian's debt interest coverage at December 31, 1977, calculated in accordance with the applicable indenture on a *total-company basis,* was 1.67 times.

The Commission devotes pages 22-32 of its Motion to arguing that coverage as a critical test in ratemaking would result in a bonanza to the common shareholders. These hypothetical and incorrect arguments, even if they were accurate, are not relevant to this case since there has never been a finding by the Commission that Appalachian's capital structure is excessively leveraged. Appalachian's return on common equity in 1977 of less than 8% is hardly a bonanza.

The Commission reasons that it would be profitable to the equity owners not only to increase the utility's debt leverage but also to borrow at higher interest rates even if lower rates were available. This reasoning hardly deserves comment. It completely ignores the fact, first of all, that the use of debt, other things being equal, is less expensive for both the customers and the Company because of tax deductibility of interest and relatively lower cost of debt compared to equity. It ignores the financial axiom

12 Motion, p. 36.

that increasing amounts of interest expose the equity holder to greater risk. It ignores the fact that the Securities and Exchange Commission requires a minimum of 30% common equity for companies subject to the requirements of the Holding Company Act and that very few electric companies have more than 40%—a rather narrow range, not the 30-90% suggested in the Commission's Table 2.[13] Moreover, it assumes the adoption of a specified coverage level, such as 2.0 times, as the *sole* test in setting rates; it further assumes that the utility's rates would be automatically adjusted to satisfy the new coverage requirements each time the utility changed its outstanding debt in any respect. Appalachian is of course not contending for any such ratemaking standard. Appalachian is contending that the ability to attract capital necessarily embraces meeting the minimum legal criteria to issue senior securities where the Company's capital structure is reasonable and its need to attract capital is unquestioned.

The Commission seems to believe that its decision was adequate to meet the coverage arguments raised by Appalachian, since the Company in fact issued long-term debt in 1975 and 1976. Here again, the Commission is misleading this Court. First, two of the five issues referred to by the Commission were refunding issues for which the Company is not required to meet a coverage test. Second and more important, the Commission fails to point out that the coverage which permitted the other three security issues was the result in part of revenues being collected subject to refund. If the Commission's final decisions had been effective at the time of these various security offerings, Appalachian would not have had the minimum legal coverage requirements necessary to be able legally to issue all of such securities.

The Commission's accusation that the Company has failed to disclose two items which materially affect cover-

13 *Id.*, p. 26.

age is wrong.[14] First, the depreciation expense ($1.4 million) was originally recorded by the Company since it was reflected in the rate application to the Commission. As a result of the Commission's decision in this case, this entry has been reversed on the Company's books. The resulting total-company coverage for the 12-month period ended December 31, 1977 was 1.67 times.[15] Second, the alleged $5 million increase in earnings which purportedly would result from a consolidated income statement would have no effect on coverage because, as the Commission should be well aware, Appalachian's coverage test must be applied on a corporate (*i.e.*, non-consolidated) basis.

Finally, the Commission's frequent suggestions that Appalachian's new rate case (filed in September 1977) will correct the constitutional deficiencies of the Commission's decision in this proceeding should be summarily rejected. As Mr. Justice Cardozo so succinctly stated, "[p]resent confiscation is not atoned for by merely holding out the hope of a better life to come." *West Ohio Gas Company* v. *Public Utilities Commission of Ohio* (No. 2), 294 U. S. 79, 83 (1935).

14 *Id.* pp. 37, 48-49.

15 For the 12-month period ended August 31, 1977, after reversing the depreciation referred to by the Commission and including the fuel expense allowed by the Commission in its decision of January 13, 1978 (Commission Appendix G), coverage was 1.87 times on a total-company basis. The jurisdictional coverage ratios, based on allocation procedure advocated in the record by the Commission's Staff, results in corresponding coverage ratios of 2.82 for the Virginia retail jurisdiction and 1.80 for the West Virginia retail jurisdiction.

III

THE FACTS IN THIS CASE BELIE THE COMMISSION'S ASSERTION THAT NO BURDEN ON INTERSTATE COMMERCE RESULTS FROM THE COMMISSION'S ORDERS; THERE ARE COMPETING DEMANDS OF STATE AND NATIONAL INTERESTS WHICH THIS COURT SHOULD RECONCILE.

The Commission's Motion characterizes this case as being concerned with "the sale of electricity of an *intrastate* nature" and therefore being a matter solely for determination by the Commission.[16] The fact that the Commission's jurisdiction is limited to West Virginia cannot insulate this decision from the requirements of the Commerce Clause. It is inconceivable that when one state's regulation directly threatens the availability of reliable electric utility service in sister states, the Commerce Clause does not protect the national interest in reliable electric service in the several states—yet this is precisely what the Commission argues.

The Commission has acknowledged facts which belie any conclusion that interstate commerce is not adversely affected by the Commission's orders. Appalachian is engaged in the interstate transmission of electric energy[17] including service to over 330,000 retail customers in Virginia, and also 21 firm wholesale customers in Virginia, West Virginia and Tennessee whose service is regulated by the Federal Energy Regulatory Commission; Appalachian, as explicitly recognized by the Commonwealth of Virginia, is facing an immediate serious inadequacy of generating capacity to serve its customers; it is engaged in a construction program exceeding $1 billion requiring massive external financing; and the Commission's orders preclude issu-

16 Motion, p. 40.

17 *Id.*

ance of additional senior securities to permit timely construction of these facilities. As stated by the Commonwealth of Virginia, given these acknowledged facts, the "cost of service to citizens of the Commonwealth may increase and the adequacy of service may be jeopardized."[18] Service to millions of customers of Appalachian's sister American Electric Power System companies throughout the Midwest would be similarly threatened.

The Commission would dismiss these facts by mistaken notions that Appalachian's demands are premature because the scheduled completion date of Appalachian's 1,300,000 Kw New Haven plant is not until the winter of 1980/81, financing is needed in each of the years 1978-81, and the possibility that other financing modes could be utilized.[19] An inability to issue senior securities in 1978 inevitably will mean that the plant will not be placed in service in time to meet Appalachian's winter demands of 1980/81. Moreover, the Commission conveniently ignores that financing in 1978 will require coverage calculations based at least in part upon earnings in 1977 and the first quarter of 1978, the level of which directly depends on the outcome of this case.

The Commission contends that, on legal grounds, its rate determinations are matters for its own discretion, matters of local concern, and not matters for scrutiny concerning their effect on interstate commerce. The law is to the contrary. As this Court has clearly stated, "ever since *Gibbons* v. *Ogden*, 9 Wheat. 1, the states have not been deemed to have authority to impede substantially the free flow of commerce from state to state . . ."[20] Clearly a considered weighing of state and federal interests is mandated.

18 Virginia Brief, p. 2.

19 Motion, pp. 44-46.

20 *Southern Pacific Company* v. *Arizona*, 325 U.S. 761, 767 (1945).

The Commission concludes with the novel argument that the effects on interstate commerce of failing to carry out new construction which is required to meet anticipated future demands is "futuristic".[21] This argument ignores the realities of the electric utility business where a minimum of six years is required to design and construct a major generating plant to meet future demands for service. The plant must be built according to a plan or schedule and the monies must be financed as they are spent; otherwise construction of the plant will have to be delayed. It is no answer to say that the effect of the delay on the Company's ability to render adequate service will not be felt until the future. As noted by this Court in *Commonwealth of Pennsylvania* v. *State of West Virginia,* 262 U.S. 553 at 593 (1923):

> One does not have to await the consummation of threatened injury to obtain preventive relief. If the injury is certainly impending that is enough.

On the present facts, it is not necessary—indeed it is foolhardy—to await failure of electric service to assess the extent of the burden on interstate commerce where implications of failure to construct needed capacity have been demonstrated without challenge on the record.

Finally, Appalachian in its aggravated condition is compelled to suggest to this Court that the current energy shortage in Ohio and elsewhere resulting from the coal miners' strike is mild in terms of the national interest compared with the power shortages that will be experienced in the 1980's if the Commission's decision is allowed to stand and a similar parochial attitude should be widely adopted by other commissions.

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21 Motion, p. 49.

CONCLUSION

This appeal presents two substantial federal questions of compelling importance in the context of the national energy crisis. The State of West Virginia seeks to justify as constitutional electric utility rates which eliminate the Company's ability to issue senior securities—a position which cannot possibly comport with *Bluefield* and *Hope*. The State of West Virginia seeks to justify as constitutional electric utility rates which so imperil the reliable supply of electricity to the Commonwealth of Virginia as to necessitate the Commonwealth's Brief to urge this Court to grant the appeal. Surely this Court should act to protect both the private interests of Appalachian and the public interests of the citizens of Virginia, West Virginia, and numerous other states.

Appalachian respectfully requests the Court to deny Appellee's Motion, and to note probable jurisdiction, or, in the alternative, vacate the final orders appealed from and remand the case for such further proceedings as the Court may deem proper.

Respectfully submitted,

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In The

Supreme Court of the United States

October Term, 1977

No. 77-979

APPALACHIAN POWER COMPANY,
Appellant,

v.

THE PUBLIC SERVICE COMMISSION
OF WEST VIRGINIA,
Appellee.

On Appeal from the Supreme Court of Appeals
of the State of West Virginia

BRIEF OF THE COMMONWEALTH OF VIRGINIA AS AMICUS CURIAE IN SUPPORT OF JURISDICTIONAL STATEMENT

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BRIEF OF THE COMMONWEALTH OF VIRGINIA AS AMICUS CURIAE IN SUPPORT OF JURISDICTIONAL STATEMENT

This brief as *amicus curiae* is filed by the Commonwealth of Virginia, by its counsel, the Attorney General of Virginia pursuant to Rule 42(4) of the Rules of this Court. The Commonwealth of Virginia respectfully requests the Court to take jurisdiction in this case.

INTEREST OF AMICUS CURIAE

Citizens of Virginia purchase large quantities of electric energy from the Appalachian Power Company ("Appalachian"). Appalachian is an electric utility serving more than 330,000 customers in the Commonwealth of Virginia

and an approximately equal number of customers in the State of West Virginia.* While Appalachian's rates are determined by several regulatory agencies, Appalachian attracts capital from external sources as a single corporate entity. Despite the authorization of fair and reasonable rates in one jurisdiction, the utility may be unable to attract the necessary capital due to an inadequate level of revenues generated by rates set by other jurisdictions. Thus, the citizens of Virginia who rely on electric service provided by Appalachian may be harmed by rate-making decisions rendered in jurisdictions other than Virginia. The Commonwealth submits this brief on behalf of its citizens.

ARGUMENT

For purposes of this brief the Commonwealth of Virginia relies upon the statement of the case contained in the Jurisdictional Statement. Assuming that the facts stated therein are proved by substantial evidence on the record of the West Virginia proceedings, this case poses substantial questions concerning the ability of Appalachian to continue to provide adequate service to its ratepayers in Virginia.

If the effect of the West Virginia decision is to preclude Appalachian from raising senior capital, and to otherwise impair its credit in the financial markets, the citizens of the Commonwealth may be adversely affected. The cost of service to citizens of the Commonwealth may increase and the adequacy of service may be jeopardized. The commerce of the Commonwealth may be similarly affected. The assurance of an adequate supply of electricity is vital to the continued economic growth and well-being of the areas served by Appalachian.

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* Rates and service affecting approximately 42 percent of Appalachian's business are regulated by the Virginia State Corporation Commission, 47 percent by the West Virginia Public Service Commission, and 11 percent by the Federal Energy Regulatory Commission.

This case presents substantial issues concerning Appalachian's constitutional right to rates which are sufficient to permit it to attract capital. See, *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944); *Bluefield Water Works & Improvement Co.* v. *Public Service Commission of West Virginia*, 262 U.S. 679 (1923). However, the concern of the Commonwealth of Virginia transcends the immediate financial integrity and credit standing of Appalachian. The Commonwealth's concern is for the well-being of its citizens who depend on electric energy generated by Appalachian. In this case, the interests of citizens of the Commonwealth coincide with the interest of Appalachian. If Appalachian is unable to obtain the capital necessary to fulfill its construction requirements, adequate service to which the citizens of Virginia are entitled may not be provided. VA. CODE § 56-234 (Supp. 1977).

CONCLUSION

As *amicus curiae*, the Commonwealth of Virginia hereby respectfully urges this Court to grant the appeal herein sought by Appalachian Power Company from The Supreme Court of Appeals of the State of West Virginia.

Respectfully submitted,

COMMONWEALTH OF VIRGINIA

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